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Recent Evolutions in the Economic and Monetary Union and the European Banking Union: A Reflection*

by Diane Fromage and Bruno de Witte

* This collection of working papers stems from a workshop on 'Current issues on EMU and EBU: A Reflection', which was organised at UM Campus Brussels on 20 May 2019.



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Introduction to the Working papers Collection -
Recent Evolutions in the Economic and Monetary Union and the European
Banking Union: A Reflection *
*Diane Fromage** and Bruno de Witte****

1. Introduction: Setting the scene

As is well known, the European Union (EU)'s Economic and Monetary Union (EMU) relies on an asymmetric structure introduced in the Maastricht Treaty (1992). The fully integrated Monetary Union in whose framework euro area Member States have attributed exclusive competence to the EU exists next to an Economic Union in which Member States' economic policies are merely coordinated.

This imbalance became particularly visible and problematic when the 2007 economic and financial crisis broke out. The need to strengthen the coordination among Member States' economic and fiscal policies, as well as the need to introduce harmonised banking prudential rules and a European Banking Union became particularly acute at that point. The crisis required the adoption of several reforms and the creation of new instruments to save the economy of Member States in difficulty, and beyond this, to ensure the survival of the euro.

As a result, the Stability and Growth Pact was reformed, the European Semester for the coordination of economic policies was introduced, a European Stability Mechanism (ESM) – preceded by several initiatives with a similar purpose – was created, and the European Banking Union (EBU) was established. Most of these reforms were adopted hastily and on a piecemeal basis at the peak of the crisis. They have affected euro area and non-euro area Member States to a different degree, among other reasons because a closer coordination is required from those states that share a common currency, and because these measures were introduced by means of the adoption of EU legislation as well as intergovernmental treaties. Not all Member States became a party to the latter. For instance, the intergovernmental Treaty on Stability, Coordination and Governance (TSCG, also known as Fiscal Compact) – which had to be adopted because of the British opposition to a revision of the EU Treaties – was ratified by all but three Member States, but not all of them are bound by the whole Treaty.¹

* This collection of working papers stems from a workshop on 'Current issues on EMU and EBU: A Reflection' we jointly organised at UM Campus Brussels on 20 May 2019. We would like to thank all the participants from academia, and especially EU and national institutions, who accepted to spend some of their time to share their views and insights, and contributed to an interesting and fruitful debate. Further thanks are owed to the Law Faculty of Maastricht University and SWOL – Universiteitsfonds Limburg, who generously sponsored the workshop.

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¹ The Czech Republic and the United Kingdom are not party to it at all, and Croatia was not an EU Member State at the time and has not become a party since it became one in 2013.

Following the adoption of what is sometimes dubbed ‘Eurocrisis law’,² the legal framework governing the EMU has hence become more complex, but also stronger. This notwithstanding, the EMU needs to be strengthened further, and the EBU remains incomplete. Many reform ideas have been put forward in recent years, and the European Commission, in particular, submitted a large set of reform proposals. Against this background, the collection of papers included in this series aims at offering a reflection on the recent evolutions in this field.

2. Current debates: Numerous reform proposals

The Five Presidents’ Report, presented in 2015 by Commission President Jean-Claude Juncker, European Council President Donald Tusk, Eurogroup President Jeroen Dijsselbloem, European Central Bank (ECB) President Mario Draghi and European Parliament (EP) President Martin Schulz³, defined some of the steps required to complete Europe’s EMU. Commission President Jean-Claude Juncker emphasised again in his 2017 State of the Union speech, *inter alia* with reference to the EMU, that ‘[w]e started to fix the European roof. But today and tomorrow we must patiently, floor by floor, moment by moment, inspiration by inspiration, continue to add new floors to the European House. We must complete the European House now that the sun is shining and whilst it still is.’⁴ Accordingly, the Commission presented its policy package on ‘Completing Europe’s Economic and Monetary Union’ on 6 December 2017⁵ in which it made mainly five proposals: 1. the establishment of a European Monetary Fund (EMF) by means of the reform of the ESM and its integration in EU law; 2. the integration in EU law of the ‘substance’ of the TSCG; 3. the creation of new budgetary instruments for the Eurozone; 4. some changes in EU funds and the Structural Reform Support Programme, and 5. the creation of a European minister of economy and finance. Next to this reform package aimed at deepening EMU, other reform proposals are currently being envisaged. For instance, the fight against anti-money laundering has become a priority in the EU, leading to the European Banking Authority being entrusted with new powers in this domain, and to the creation of a new, dedicated, authority being envisaged.⁶ The strengthening of the international role of the euro has also been recurrently set as a priority, while the completion of the EBU, and notably the creation of a deposit insurance guarantee scheme, is regularly debated. Furthermore, existing cohesion policy instruments have increasingly been used with a view to foster economic stability.

² See on this, for instance, T. Beukers, C. Kilpatrick and B. de Witte (Ed.) *Constitutional Change Through Euro-Crisis Law*, Cambridge, Cambridge University Press.

³ J.-Cl. Juncker et al., Five Presidents’ Report ‘Completing Europe’s Economic and Monetary Union’, 2015, available at : https://ec.europa.eu/commission/sites/beta-political/files/5-presidents-report_en.pdf.

⁴ J.-Cl. Juncker, State of the Union Address 2017, 13 September 2017, available at : https://europa.eu/rapid/press-release_SPEECH-17-3165_en.htm.

⁵ Available at : https://ec.europa.eu/info/publications/economy-finance/completing-europes-economic-and-monetary-union-policy-package_en.

⁶ See on the Commission’s stance on anti-money laundering within the EU : European Commission, Communication from the Commission to the EP and the Council, ‘Towards better implementation of the EU’s anti-money laundering and countering the financing of terrorism framework’, COM(2019) 360 final, 24.7.2019.

Brexit, and the United Kingdom (UK) generally, have additionally had a significant influence in the course of recent developments in the fields of EMU and EBU for several reasons. Firstly, as mentioned above, the UK has been a fierce advocate of the interests of the non-euro area Member States; secondly, the uncertainties related to the outcome of the Brexit referendum, and the Brexit decision itself, have taken much of the EU's resources and attention; thirdly, the prolonged extraordinary circumstances provoked by the ever-lasting Brexit negotiations have resulted in the emergence of new informal institutional configurations known as 'inclusive formats' (that is, meetings of the EU-27 without the UK).

3. Introducing the contributions

Whilst some of the proposed reforms and changes have already been adopted or have already intervened, others appear to have been abandoned, or are still very much under discussion. In a stocktaking exercise, the contributions included in this series of papers examine the course of those negotiations, their outcome and the likely (legal) consequences of the adopted measures. They consider how the December package has evolved 18 months after it was proposed (Paul Dermine), and analyse two of its components in particular: the Euro area budget (Marijn van der Sluis) and the use of the ESM as a backstop to the Single Resolution Fund (SRF; Jean-Paul Keppenne, Tim Maxian Rusche and Laura Estrella Blaya). The relationship between cohesion policy and EMU is also studied (Leo Flynn), as is the opportunity to go beyond the principle of 'institutional unity' with a view to accommodate euro area-specificities in the EU's institutional landscape (Diane Fromage). The series concludes with a reflection on the international role of the euro (Klaus Tuori).

In his analysis, Paul Dermine shows that the December package is based on the premise that unity has to be maintained by avoiding the further differentiation between euro area and non-euro area Member States and that the Commission clearly seeks to streamline and 'communitarise' the instruments adopted during the crisis. He also highlights that one of the underlying assumptions is that any reform must be enacted without any change to the Treaties, and that the Commission's ambitions are rather limited, and to a large extent in strict continuity with the reforms previously enacted. Despite these rather low-key ambitions, most proposals have not flown, owing to a political context that became less favourable soon after the Commission issued its package. In Paul's view the 'failure to deliver can [however] be best explained by structural disagreements as to the nature of the EMU, and its cardinal principles, that Eurozone Member States and EU institutions have so far failed to overcome'. Paul furthermore describes how the ESM has remained outside the EU legal framework, though it will soon acquire a new EU-related task of providing a backstop to the SRF. Relatedly, Jean-Paul Keppenne, Tim Maxian Rusche and Laura Estrella Blaya focus on the difficulties arising from this combination of an intergovernmental instrument, the ESM, with an EU mechanism, the SRF. They first recall the legal limitations for the conclusion of intergovernmental treaties outside the EU legal framework, before turning to the challenges that the need to safeguard confidentiality, to preserve the autonomy of EU law and ensure

accountability bring about. In his analysis of the evolution of the December package, Paul Dermine also comments on the evolution of the proposed euro area budgetary instrument. This instrument is examined more in-depth by Marijn van der Sluis who sheds some light on the potential legal issues related to the (now likely) creation of the Budgetary instrument for competitiveness and convergence (BICC). Marijn not only provides a critical analysis of the BICC negotiations and the underlying tensions that they have revealed; he also seeks to determine whether it could swiftly become a fully-fledged euro area budgetary instrument if a new crisis were to occur. He concludes that ‘the predominance of the MS [Member States] in the setup and functioning of the BICC [...] would allow for a rapid expansion of the instrument under the right political circumstances. At the same time, it is [, in his view,] doubtful whether in the long-term the reliance on the MS [Member States] for the functioning of EMU is sustainable, in lieu of relying on strong, democratic institutions on the European level’.

The two papers by Diane Fromage and Leo Flynn are not related to the December Package. Instead, they both analyse two sets of developments that have already happened. Indeed, Diane Fromage considers the issue of the accommodation of the specificities of the euro area within the EU institutions in a context in which it is unlikely that all non-euro area Member States will adopt the common currency in the near future, and in which new Eurogroup and Euro Summit ‘inclusive formats’ have arisen in the wake of Brexit. In doing so, Diane examines the main EU institutions in turn and concludes that even if there is no straightforward answer to this dilemma, there is a need to strengthen transparency and democratic accountability by *inter alia* reinforcing national parliaments’ collective participation. Leo Flynn in turn concentrates on the link between cohesion policy and the deepening of the EMU, and analyses both older and recently proposed instruments. He concludes that cohesion policy has been successfully used to try and remedy some of the shortcomings of the economic policy framework.

Klaus Tuori’s critical views on the Commission’s goal to strengthen the international role of the euro conclude this series of papers. He examines both the economic rationales of the Commission’s proposal, as well as the division of responsibilities and competences in pursuing this goal.

He shows for instance that the Ecofin Council should arguably be the ultimate decision-maker in this field, working together with the ECB. He also highlights the need to establish the economic rationale for expanding the international role of the euro more firmly.

4. Looking ahead: What future for the EMU?

The papers included in this collection clearly show that, so far, progress in the reform discussions has been slow, particularly with regard to the Commission’s December Package. Besides the reasons that have already been mentioned, this result might also be unsurprising as some of the reforms proposed by the Commission were arguably aimed at putting those items on the EU leaders’ agenda rather than at leading to an immediate change; this most clearly applies to the proposal of the creation of a European finance minister for example.

In the reforms that have successfully been enacted (or at least negotiated), the path taken during the crisis has mostly been followed. On the whole, Member States have not sought to greatly add coherence and more legibility to the existing legal framework, and they have also not empowered EU institutions further by repatriating the ESM Treaty and the TSCG in the EU legal order, as the Commission had proposed. Instead, they have agreed on reforms which have continued to rely largely on intergovernmental instances.

As mentioned above, the uncertainty of Brexit certainly makes it hard(er) to predict how the EMU and the EBU are going to evolve in the future. If Brexit does happen, the only Member State which will (formally at least) be bound to remain outside of the euro area will be Denmark, a smaller Member State. Additionally, the shares between euro area and non-euro area Member States in the EU's GDP will shift leading to the non-euro area Member States contributing to a very limited extent to the EU's GDP. It is, however, not only the uncertainty related to Brexit that makes it difficult to know how and if the strengthening of the EMU and the completion of the EBU are going to be pursued. Also the evolution of the German political landscape, and the outcome of the federal elections scheduled for September 2021 could play an important role in this regard, as could the pressures exercised by the rise of populism observable in several EU Member States.

At any rate, the questions discussed in this collection can be expected to remain high on the new European Commission's agenda, thereby calling for further close monitoring in the upcoming period.

The Commission's December Package 18 months later

*Paul Dermine**

1. Introduction

On December 6, 2017, the European Commission published a set of legislative and non-legislative proposals, quickly labelled by the Brussels bubble as the ‘Saint Nicholas’ package. Building upon earlier institutional reflections (most notably the 2015 Five Presidents’ Report and the Commission’s own Reflection Paper on Economic and Monetary Union (EMU) Deepening), and seeking to take advantage of the window of opportunity opened by Macron’s election, the package consists in a bundle of initiatives all geared towards the completion of the EMU. In a nutshell, the package consists in legislative proposals on the repatriation of the European Stability Mechanism (ESM) and the Treaty on Stability, Coordination and Governance (TSCG) within the EU legal order. It envisions a strengthening of the autonomous budgetary capacity of the Eurozone, through a consolidation of the Structural Reforms Support Programme and the setting up of a new stabilization mechanism (entitled the European Investment Stabilization Function). It also strives to streamline the institutional architecture of the Eurozone, by creating a new position of European Minister for Economy and Finance, which would merge the Commission vice-presidency in charge of Eurozone matters with the presidency of the Eurogroup. Finally, the package envisages punctual modifications to the Common Provisions Regulation¹

This Working Paper aims at critically assessing how the Package has fared in the first 18 months after its publication. It will first come back to the approach favored by the Commission in the Package, and shed light on the ambitions it is to serve, and its intrinsic limits. The paper will then provide an overview of the institutional reactions the Package and its various proposals have triggered, both within the other European Union (EU) institutions, and in European capitals. This overview will primarily underline major difficulties to move forward on any of the proposals made by the Commission. The paper will end with an attempt to identify the key factors that may explain the current deadlock.²

2. The Package and its Underlying Narratives

Following the official narrative presented by the Commission, the entire package revolves around three core guiding principles. First, unity. The package can be read as an implicit attempt to settle the debate

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¹ Regulation No. 1303/2013 defines the common rules applicable to the European Structural and Investment Funds. The modifications sought to enable the use of the performance reserve to support the implementation of structural reforms identified in the European Semester process.

² Time of writing: August 2019.

about further Eurozone differentiation in favor of uniform integration. The package indeed presents a high degree of openness towards the ‘outs’, and clearly seeks to avoid exclusivity and antagonism. Secondly, the package is geared towards improving the overall efficiency of the EMU which, from the perspective of the Commission, implies the full supra-nationalization of the new governance structures set up during the crisis, and the streamlining of the various regulatory instruments it gave birth to. There is a clear aspiration towards a return to constitutional normalcy and Treaty orthodoxy, and the will to correct the institutional and normative anomalies the crisis inevitably produced. This endeavor is of course best evidenced by the attempts to repatriate the ESM and the TSCG within the EU legal order. Finally, the package is also geared, so the Commission claims, towards the further democratization of the governance of the EMU: increased responsibility, accountability and transparency are indeed put forward as core concerns by the Berlaymont.

Beyond the official narrative presented by Brussels, a closer and more critical analysis of the package reveals other driving forces, that are not explicitly acknowledged by the Commission, but seem nonetheless to have firmly structured the entire exercise. We identify two main force lines. On the one hand, the entire package is premised on the idea that treaty revision is, as a matter of principle, not even to be considered, and that reforms can only be envisaged within the limits of the existing Treaties. However reasonable it may be, such premise naturally limits the very ambition of the entire initiative in a significant manner. In that sense, the December package very much continues the mindset which overall has prevailed throughout the crisis: reforms and transformations can only be considered *à droit primaire constant*. It does not mean that the margin of manoeuvre left by the Treaties is not fully exploited (it actually, to a large extent, is), but it implies that there is no pretention for a more fundamental rethinking of the structuring features of the EMU. On the other hand, the package does not display any attempt to meaningfully break with the legacy of the crisis. On the contrary, in that it confirms key elements of that legacy, it displays a high level of path-dependency. The ambition revealed is quite low; and the package very much limits itself to adaptation and adjustment, at the expense of genuine innovation or invention. It does certainly not attempt to shift the overall trajectory of the EMU. On the contrary, it very much confirms the *status quo*, with marginal adjustments. A good example of this is the ‘TSCG Directive’ proposal. The repatriation of the Fiscal Compact in the EU legal order would surely have constituted an ideal opportunity to rethink the entire fiscal rulebook of the Eurozone, which according to many observers, has become highly dysfunctional overtime. This opportunity was clearly not seized, as the proposed directive mainly limits itself to copy-pasting the core provisions of the TSCG in an EU instrument.

The package is the outcome of a difficult reflection process within the Commission, at the end of which realism and restraint seem to have prevailed. Do not get me wrong: the package does put forward a number of important and welcome changes. However, the institutional architecture inherited from the

crisis is widely preserved, and its founding features, such as its rules-based nature, the centrality of the strict conditionality principle or the prevalence of the surveillance model (and the correlated negative approach towards economic and fiscal integration), clearly confirmed. In that it limits itself to confirming the *status quo*, the package has been criticized for its lack of vision and ambition by commentators for whom the political and economic context was ripe for a deeper reorientation of post-crisis EMU. Along these lines, a noted editorial in the *Common Market Law Review* has described the package as a mere ‘tinkering exercise’.³

3. The December Package 18 months later: *Tout ça pour ça?*

Where do we stand 18 months later? In the following paragraphs, we provide a general overview of the progress made (or not made) on each of the components of the Package.

As a general rule, it must be said that the negotiating context rapidly deteriorated. The wave of Eurooptimism set in motion by Macron’s victory, and on which the Commission had tried to capitalize with its December Package, quickly came to a halt. The weakening of Merkel’s position in Germany disrupted the Franco-German dynamics, as best exemplified by the relatively unambitious Meseberg Declaration in June 2018. The rise of the so-called ‘New Hanseatic League’, a group of fiscally conservative countries opposed to further solidarity, led by the Netherlands,⁴ further deepened the division between Member States on the future of the EMU. At home too, Macron’s star began to wane, as his national reform plans were met with strong popular opposition (most notably from the Yellow Vests movement), further damaging his credibility on the European stage. The reform momentum was thus quickly lost, and from the end of 2018 onwards, it became clear that EMU reforms along the lines of the Commission’s proposals (and the French vision outlined in the Sorbonne and Athens speeches) would be difficult to obtain. The meager results of the last two Euro summit meetings in December 2018 and June 2019 do confirm just that. It now remains to be seen if the results of the last European elections, and the upcoming round of political appointments, will exacerbate the deadlock, or offer a way out of the conundrum.

In such an unfavorable political environment, it has been hard for the Commission to make its Package proposals fly. It is indeed quite notable that none of its major components has been adopted, or is about to be. The reaction of other ‘supranational’ EU institutions (Parliament, European Central Bank (ECB),

³ Editorial Comments, ‘Tinkering with EMU’, *CMLR*, 55(3), pp. 709-718.

⁴ The League defends a vision of the EU centered on trade and market issues. With regard to EMU, strong emphasis is placed on compliance with common fiscal and economic rules, national responsibility and collective risk-sharing. The foundational document of the League can be found here: <https://vm.fi/documents/10623/6305483/Position+EMU+Denmark+Estonia+Finland+Ireland+Latvia+Lithuania+the+Netherlands+and+Sweden.pdf/99e70c41-6348-4c06-8ff8-ed2965d16700/Position+EMU+Denmark+Estonia+Finland+Ireland+Latvia+Lithuania+the+Netherlands+and+Sweden.pdf.pdf>.

Committee of the Regions, European Economic and Social Committee) has been rather positive, as their vision about the future of the Eurozone seem to be broadly aligned to that of the Commission. It is in the Council that discussions have stalled, as Member States have so far proven unable to overcome fundamental disagreements (see *infra*).

The European Monetary Fund (EMF) Regulation proposal, and the idea of a repatriation of the ESM within the EU institutional architecture, has been positively welcomed, although not without certain reservations, by most other EU institutions. The European Parliament, the ECB and the European Court of Auditors, most notably, have explicitly voiced their enthusiasm. The transformation of the ESM into an EU body has however been met by strong resistance in the Council, where the proposal is currently still stuck. The ESM itself has made its opposition to the idea very clear. There however seems to be consensus about the need to amend the tasks and internal functioning of the ESM, most generally along the lines suggested by the Commission. Upcoming changes⁵ have been compiled in an ESM term-sheet, which has been validated by the December 2018 Euro summit, and should soon be implemented through a revision of the ESM Treaty.⁶

The reactions to the Commission proposals for new Eurozone budgetary instruments⁷ have been equally contrasted. With its two proposals, the Commission had already shown restraint and pragmatism, and tried to strike a compromise between the competing visions as to the size and rationale of a future Eurozone budget. Each proposal indeed follows a logic of its own. The ‘Structural Reforms Support Programme’ (SRSP) consists in a set of financial incentives for Member States willing to implement the growth-enhancing structural reforms recommended by the EU in the framework of the European Semester.⁸ It is primarily about nudging the Member States to pass the reforms that would strengthen the resilience of their economic and social structures, following a ‘cash for reform’ logic. The second instrument, the ‘European Investment Stabilization Function’ (EISF), obeys a different logic: it provides EU resources to Eurozone Member States in order to help them attenuate the effects of large asymmetric

⁵ See Term sheet on the European Stability Mechanism reform, 4 December 2018, available at https://www.consilium.europa.eu/media/37267/esm-term-sheet-041218_final_clean.pdf. Among others, the term-sheet foresees that the ESM will provide the fiscal backstop to the Single Resolution Fund in the form of a revolving credit line; it enhances the effectiveness of precautionary instruments; it increases attention to debt sustainability issues and provides for a more self-standing role of the ESM in its own operations.

⁶ In that regard, see already the ‘Draft revised text of the treaty establishing the European Stability Mechanism as agreed by the Eurogroup on 14 June 2019’, available at <https://www.consilium.europa.eu/media/39772/revised-esm-treaty-2.pdf>.

⁷ With regard to budgetary instruments, the package was delivered in stages. While instruments were already announced in a Communication in December 2017, they were further materialized in two legislative proposals tabled in May 2018.

⁸ This proposal is to be discussed in the framework of the negotiation of the 2020-2027 multiannual financial framework. See European Commission, ‘Proposal for a Regulation of the European Parliament and of the Council on the establishment of the Reform Support Program’, 31.5.2018, COM(2018)391final.

shocks they cannot manage on their own.⁹ The function would work as a common insurance geared towards the protection of public investment (the item which tends to be cut first in case of crisis): Eurozone Member States would make yearly contributions in order to build up assets in good times, and would receive transfers if faced with downturns (identified by sudden rises in unemployment). In so doing, the function would help national authorities absorbing large shocks, and prevent contagion and negative spillovers to other countries.

Obviously, the two proposals do not pursue a similar rationale, and seem to be designed to realize each a different kind of stabilization, with various levels of solidarity. While the first type of budgetary instruments seeks to promote socio-economic convergence and resilience, and incentivize responsibility at home, the second type of instruments would serve a more classic macroeconomic stabilization function, as it would seek to mitigate and absorb, through fiscal transfers, the effects of asymmetric shocks hitting certain sub-units of the currency union. The SRSP is dominated by the logic of conditionality, as transfers are not automatic but depend on compliance with EU prescriptions on economic and fiscal policy, and must be expressly validated by Union institutions. The EISF, as it serves a shock-absorbing function, is run on a quasi-automatic basis, and entails a much more significant amount of funds. These fundamental differences between the two Commission proposals very well explain the contrasted fates they experienced over the past few months. Discussions on EISF have so far stalled, despite strong support in the European Parliament, the Committee of the Regions and the European Economic and Social Committee.¹⁰ There indeed seems to be a clear lack of political appetite for further fiscal solidarity on the part of certain Member States (especially those forming the Hanseatic League). There has however been more interest for the (much more limited) Structural Reform Support Programme. In the meantime, it has been relabeled ‘budgetary instrument for competitiveness and convergence’ (BICC) by the Euro summit, which in December 2018, tasked the Eurogroup to work on the design and modalities of the instrument.¹¹ It is in the framework of these ongoing discussions that the French and German governments have tabled a joint proposal for a Eurozone-specific budgetary instrument, which closely resembles that put forward by the European Commission, with a stronger intergovernmental tint.¹² In June 2019, the Eurogroup has produced a first term-sheet on the BICC, but the latest Euro summit failed to deliver political compromise on the instrument.¹³ It thus remains to be

⁹ See European Commission, ‘Proposal for a Regulation of the European Parliament and of the Council on the establishment of a European Investment Stabilisation Function’, 31.5.2018, COM(2018)387final.

¹⁰ These three institutions have indeed positively welcomed the proposal, and asked for more automaticity, and more ambitious financial means.

¹¹ Euro summit, Statement of 14 December 2018, EURO503/18, § 4.

¹² Franco-German proposal, ‘Eurozone budgetary instrument – possible ways forward after the December 2018 summit’ (21 February 2018), < <https://www.euractiv.com/wp-content/uploads/sites/2/2019/02/French-German-Contribution-on-a-Eurozone-Budgetary-Instrument-2.pdf>> accessed on 8 March 2019.

¹³ See Smith-Meyer, B., ‘Rutte declares Eurozone budget dead, Macron hails its good health’, Politico, 21 June 2019, available at: <https://www.politico.eu/article/rutte-declares-eurozone-budget-dead-macron-hails-its-good-health/>. In the meantime, see European Commission, ‘Proposal for a Regulation of the European Parliament and

seen if the Eurozone budget will ever see the light of day. What is clear however is that if it is ever set up, it will not serve a macroeconomic stabilization function in the classic sense of the term. It will be a limited budgetary instrument, geared towards risk-reduction, focused on structural reforms, and competitiveness and convergence at home, organized on a non-automatic basis, and relying on a complex eligibility regime. A new sort of economic conditionality, based on incentives rather than sanctions, on carrots rather than sticks. Far from what the Commission had in mind when designing the December Package.

Discussion on the 'TSCG Directive' proposal have also not produced any tangible results yet, in spite of the proposal's limited ambition and rather uncontroversial content. Again, the European Parliament and the ECB have generally welcomed the proposal, and expressed legitimate concerns.¹⁴ Discussions in the Council have so far not made much progress,¹⁵ but such procrastination may well be explained by the fact that the Council is waiting for the upcoming Commission review of the Six-Pack and Two-Pack. More fundamentally, the TSCG is an instrument that overtime has lost much of its political and legal relevance. It is therefore no surprise that its incorporation into the EU legal order is not perceived as a top priority.

Finally, in its December Package, the Commission also proposed to merge the positions of Eurozone Commissioner (and Commission's vice-president), President of the Eurogroup and Chair of the ESM Board of Governors into one single European Ministry of Finance, placed under the Commission's roof. According to the Commission, such new practice could be implemented under the current legal framework, hence the absence of any formal legislative proposal.¹⁶ It remains to be seen if the Commission's suggestion is followed upon when the next Eurogroup President is appointed (the next vote should occur at the end of 2020). Despite explicit support from the European Parliament (because of the increased accountability that the proposal would allow), Member States have shown a quasi-unanimous lack of interest for the Commission's initiative, in view of the inevitable centralization and supranationalization it would produce.¹⁷ Wait and see, but it very much looks like the Minister project is a stillborn one.

of the Council on a governance framework for the budgetary instrument for convergence and competitiveness for the euro area', 24.7.2019, COM(2019)354final.

¹⁴ Among others, the European Parliament has suggested a change of legal basis (which would allow avoiding unanimity voting), and the ECB has warned against the risk that text may ultimately add further confusion to the fiscal discipline rather than simplifying it.

¹⁵ Certain specific opinions from the Legal Service were requested, on the participation of non-Eurozone member States and on the future status of the TSCG in case of adoption of the Directive.

¹⁶ The Commission merely issued a Communication.

¹⁷ On top of that, the initiative has raised many doubts as to its constitutional validity. In this regard, see Patrin, M., Schlosser, P., 'The European Finance Minister and the EMU Reform Conundrum', *Capital Markets Law Journal*, 2019, 14(2), pp. 274-291.

4. Explaining the Current Deadlock – A Modest Attempt

How can we explain the current deadlock? Why did discussions on the policy package put forward by the Commission, to a large extent, stall? Elements of pure political context, such as the isolation of Macron on the EU stage, the emergence of the Hanseatic League, or a relatively low sense of emergency, did undeniably play a role. One may also evoke the fact that the Package, although evidently building upon the Five Presidents Report, came in very quickly, without any preparatory discussions or interinstitutional consultations having taken place at EU level.¹⁸ In the following paragraphs, we show that such failure to deliver can be best explained by structural disagreements as to the nature of the EMU, and its cardinal principles, that Eurozone Member States and EU institutions have so far failed to overcome.

4.1. Intergovernmental vs Supranational Governance of the Eurozone

The first of these divisions is quite classic, but is more pregnant than ever under the current discussions. It relates to the opposition between proponents of a supranational approach to EMU governance and EMU reform, and supporters of an intergovernmental perspective. This antagonism is clearly perceivable, with regard to both the *process* through which these reforms are to be brought about, and the actual *substance* of the institutional changes contemplated.

As to the reforms process, first. The very launch of the December package reveals a clear will of the Commission to put itself, and the Community method, at the center of the political game. This attempt to regain the upper hand on EMU reform after a long period of crisis intergovernmentalism participates to this return to normalcy and orthodoxy that we have described in the above. In this endeavor, the Commission has found strong support within the European Parliament, and has received backing from the ECB, the Committee of Regions, the Economic and Social Committee, and from those Member States most enthusiast about EMU deepening (such as France, Italy or Spain). However, the Commission's monopoly on reform initiative has been contested by proponents (such as the Netherlands, Germany and other members of the so-called new Hanseatic League) of the intergovernmental track, which have sought to consolidate the 'international law' components of the Eurozone's governance framework. This is best epitomized by the recent developments regarding the Commission's EMF proposal. As shown in the above, the central ambition of the proposal is to bring the ESM back within the institutional framework of the EU.¹⁹ It therefore primarily focuses on making this possible, by introducing the necessary institutional and legal adjustments. In parallel, and

¹⁸ This very much conforms to the legislative timeline set up by the Treaties, and can be best explained by the Commission's recent experience of the Six-Pack and Banking Union discussions, in which it was, as a legislative initiator, very much sidelined. However, such strong will to occupy the political space and control the legislative tempo can explain the backlash currently experienced in the Council.

¹⁹ In that regard, it should be noted that the ESM Treaty, unlike the TSCG, does not comprise a so-called 'repatriation clause'.

incidentally, to this repatriation effort, the proposal also puts forward a number of more or less minor material changes to the functioning of the ESM, most notably on the common backstop to the Single Resolution Fund (SRF) and precautionary instruments. It is interesting to note that the Commission proposal is currently suspended in limbo, as there is a clear lack of appetite in the Council for the repatriation of the ESM, and its transformation into an EU body (the central element in the Commission's project). However, recent diplomatic discussions have brought about intergovernmental agreement on most of the material changes put forward by the Commission, which are to be introduced soon via a revision of the ESM treaty.²⁰ It is as if the Commission proposal had been emptied of its substance along the way. Its central innovation was tossed aside, while its secondary suggestions were preserved. More specifically, they have been taken over by the States, and introduced in a purely intergovernmental formula. In a certain manner, the return to normalcy is denied, and the reconnection with the community method rejected. More fundamentally, the fate of the EMF proposal suggests that in EMU matters the community method can easily be captured, or at least diverted, by the intergovernmental method. The competition between methods thus persists in the post-crisis era, and comes out as a more enduring feature of EMU policy. There seems to be a strong will to perpetuate the intergovernmental components of the Eurozone system, if not further consolidate them. This is very much promoted by governments that want to maximize State control on the pace and orientation of EMU reforms and, more interestingly, by the ESM itself, which has progressively gained autonomy within the Eurozone institutional system, and seems to have forged itself an ambitious vision for its own future.

In substance as well, the prospect of further communitarisation of Eurozone governance has been greeted quite coldly, as best evidenced by the case of the EMF proposal, or the Commission proposal on a stabilization function. There is of course the loss of vetoes that the move away from unanimity would entail. There is also the transfer of the main *loci* of accountability (political, legal, financial) to the supranational level, at the inevitable expense of national institutions, that will generate strong opposition. Interestingly in that context, one can also not help sensing a growing distrust vis-à-vis the European Commission. Several Member States, supported by other EU bodies and institutions (such as the ECB or the European Fiscal Board), have questioned the ability of the Commission to neutrally enforce the collective economic and fiscal discipline of the Eurozone, and to act as the guardian of a rules-based EMU. The issue of the politicization of the EU Commission in the EMU context is not new, but it has certainly gained momentum in several capitals over the past few years. Despite recent attempts from the Commission to re-assert its credibility (most notably in the recent Italian budget crisis), this suspicion is still very much there. It certainly explains some recent proposals to move surveillance and

²⁰ The Eurogroup and Euro summit meetings in December 2018 and June 2019 confirmed that a consensus had been secured on a so-called term-sheet on ESM reform. Treaty revision should normally occur by December 2019.

enforcement powers in the field of economic and fiscal policy away from the Commission.²¹ *A fortiori*, it is behind the current reluctance of many to further empower the Berlaymont by transferring additional powers from intergovernmental bodies to the Commission.

4.2. Responsibility or Solidarity? Risk-Reduction vs Risk-Mutualization

The second division relates more specifically to the content of the reforms to be passed and the fundamental orientation they should be given. Ultimately, it begs the question of the final destination, the ultimate telos of the EMU. This division opposes the proponents of risk-reduction and those in favor of increased risk-sharing and risk-mutualization.

According to the former, the action of the EU, in the field of economic policy or financial policy, ought to be primarily geared towards convergence, sustainability, and the elimination of risk factors. The approach is primarily regulatory. Final decision-making powers and responsibilities still lie at the national level, and the EU's role is limited to inducing the necessary reforms via legal rules, administrative surveillance, and a diversified set of positive and negative incentives. Mutual exposure and collective solidarity are kept to a minimum.

The latter favor a much more far-reaching understanding of the powers of the EU in the field. The interdependencies and spillovers that the sharing of the single currency inevitably entails would call for the set-up of positive means of action at EU level, and a move beyond a strictly regulatory approach. The recognition of the collective, and not purely national, nature of goods such as financial stability, fiscal sustainability or competitiveness, would lead to the erection of joint responsibilities, to be governed politically at the supranational level. The ambition is thus to match the interdependencies created by the euro with appropriate forms of solidarity.

However central and structuring the debate between risk-reduction and risk-sharing is, one should beware of overstatements. For example, it is often reduced to an opposition between French dirigisme and German ordo-liberalism, and more generally, between Southern catholic Europe and Northern protestant Europe. If there is some truth in this, it is also in many regards much of an oversimplification. Moreover, both concepts are not mutually exclusive, and tend to be combined in concrete reform proposals. The question is therefore not whether we should have risk-reduction or risk-sharing, but how

²¹ The suggested expansion of the European Fiscal Board, created in 2017 to oversee the application of the EU's fiscal framework, can be read along those lines. Other proposals to empower the ESM, allegedly more objective and apolitical than the Commission, in the field of fiscal supervision, also come to mind. See for example Schäuble's non-paper (Schäuble, W., 'Non-paper for paving the way towards a stability union', October 2017, < <https://scienzepolitiche.uniroma3.it/fmasini/wp-content/uploads/sites/41/2018/10/Schauble-2017-Non-Paper.pdf>> accessed 3 June 2019), or Fuest's proposals (Clemens Fuest, 'A three-step plan for a better European Monetary Fund', *Euractiv*, 5 January 2018, < <https://www.euractiv.com/section/economic-governance/opinion/a-three-step-plan-for-a-better-european-monetary-fund/>> accessed 3 June 2019).

much we should have of each. The composition of the policy mix is therefore the crux of political negotiations. The deep overhaul of the EMU carried out in the aftermath of the Eurocrisis has primarily put the emphasis on risk-reduction (the reform of fiscal and economic governance, the adoption of the Single Rule Book and the supranationalization of financial supervision, the politics of strict conditionality), even though certain risk-sharing mechanisms were also established (think of the ESM and a new financial assistance function, the creation of the SRF, or the action of the ECB). Equally decisive is the issue of sequence. There seems now to be a broad consensus that ultimately the Eurozone ought to be endowed with strong solidarity mechanisms, and that risk-sharing ought to be substantially deepened. However, more divisive is the question of the amount of risk-reduction that needs to be achieved before further risk-mutualization can be envisaged.

The pregnancy of the ‘risk-reduction versus risk-sharing’ divide in the current negotiations is best illustrated by two reform projects under discussion at the moment. First, the talks about the creation of Eurozone-specific budgetary instruments. Recent discussions have revealed a fundamental disagreement as to the objective that such instruments should serve. According to a first view, clearly based on risk-reduction, these funds would finance reforms strengthening the convergence, resilience and competitiveness of national economies, and would serve as additional incentives to comply with the collective fiscal and economic discipline of the Eurozone. Under such a view, their disbursement would not be automatic, as it would require a validation of the reforms hence financed by the EU, and would be conditional upon compliance with the rules of the Stability and Growth Pact. Following a second approach, clearly tilting towards risk-sharing, these budgetary instruments would serve a macroeconomic stabilization function. The general idea is that economic shocks of a certain magnitude, identified through objective criteria (an economic downturn of a certain scope, a surge in unemployment of X points, ...), would, automatically and unconditionally, trigger a centrally managed fiscal reaction to promote counter-cyclical interventions. Naturally, one is quick to understand that, depending on the logic favored, the related questions of the size of the financial means required by the contemplated budgetary instruments and of their origins will receive different answers. The promotion of national reforms fostering economic convergence can already be considered with relatively limited funds, originating from national contributions, whereas a credible Eurozone shock absorption function necessarily demands firepower equivalent to several points of Eurozone GDP, that could only be raised through own resources or European taxes. The ambitious vision of Macron for a Eurozone budget clearly belongs to the second approach. So does, although in a less clear-cut manner, the recent Commission’s proposal on an investment stabilization scheme. However, these projects have met the opposition of States for which budgetary instruments could only serve a risk-reducing and disciplinary function. The limited progress made on the Commission proposal, the most recent Franco-German proposal and Eurogroup deliberations suggest that this view is dominating the debates.

Second, the difficulties of the Member States to reach agreement on the finalization of the Banking Union (BU) can also very much be explained by their inability to solve the ‘risk reduction v. risk sharing’ conundrum. On the risk-sharing side, some progress has recently been made on the fiscal backstop to the SRF, but discussions on the third pillar of the BU, i.e. the European Deposit Insurance Scheme (EDIS), remain difficult. Whereas the very principle of a third pillar is not seriously contested, the timing for its establishment certainly is. It is therefore primarily an issue of sequencing. Considerable efforts have already been made in terms of risk-reduction in the banking sector (non-performing loans reduction, minimum requirements for own funds and eligible liabilities build-up, insolvency regime, ...). Sufficient to move on for some, not for others, who consider that further efforts must be carried out to meet the pre-conditions required for the setting up of the EDIS. A fundamental disagreement which explains the many postponements in this file.

5. Conclusion

It is an understatement that the December Package, since its launch by the Commission in December 2017, has not fared well and did not produce the results expected. It has lost most of its momentum and, if the negotiation process is still alive and kicking, it is now firmly in intergovernmental hands. The reasons behind this failure are manifold. Undeniably, context did play an important part. The window of opportunity the Commission planned to benefit from, rapidly closed, and the political climate swiftly deteriorated. But more fundamentally, political discussions about the Package so far have revealed structural disagreements between EU institutions, and among Member States, as to the reform method that ought to be favored, and as to the substance of the changes to be implemented. At the moment, there seems to be irreconcilable understandings of what the EMU is to become on the long-term, and how it should be brought about. As a result, the Eurozone has so far proven unable to move beyond the status quo. Minor reforms were adopted, but States and EU institutions have never truly seemed ready to transcend their divisions to carve out a common vision. The crisis legacy was broadly consolidated, leaving many fundamental questions unanswered.

A Euro area budget: another seedling?

*Marijn van der Sluis**

1. Introduction

This working paper examines the recent proposals for a euro area budget as part of the ongoing efforts to reform the euro.¹ In June 2019, the Eurogroup reached consensus on a ‘term sheet’ regarding a new budgetary instrument, the *Budgetary Instrument for Competitiveness and Convergence* (BICC), whose immediate history can be traced back to the 2015 report by the five Presidents of the EU (European Commission, European Council, Eurogroup, European Central Bank (ECB), European Parliament (EP)).² That report set the agenda for the reforms for the post-crisis era and included several small reform proposals, such as the creation of a system of national competitiveness authorities and a European Fiscal Board, as well as several larger proposals, such as a ‘macroeconomic stabilization function for the euro area’. This would be due in the ‘stage 2’ outlined in the report, i.e. between June 2017 and 2025.

The stabilization function for the euro area would (partly) fulfill a long-standing desire to ‘complete’ the euro. The original ‘imbalance’ of the Economic and Monetary Union (EMU), with a strongly developed monetary union and a weakly developed economic union, is seen by many as a lead cause of the euro crisis. By elevating monetary policy to the European level and keeping fiscal and economic policy largely decentralized, the Member States (MS) lost their tools to combat so-called asymmetric shocks, i.e. an economic downturn that affects only a group of MS. Even though the euro-crisis led to an overhaul of EMU, most of the measures taken during the euro-crisis have been targeted at crisis fighting, rather than crisis prevention. A European stabilization function would offer targeted support

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¹ A number of commentaries have appeared regarding various proposals on the euro area budget. See Paul Craig and Menelaos Markakis, “EMU Reform,” in *The EU Law of Economic and Monetary Union*, ed. Fabian Amtenbrink and Christoph Hermann, 2019; Richard Crowe, “Is a Separate Eurozone Budget a Good Idea?,” *ADEMU Working Paper Series* WP 2018/120 (2018); Luca Lionello, “Establishing a Budgetary Capacity in the Eurozone. Recent Proposals and Legal Challenges,” *Maastricht Journal of European and Comparative Law* 24, no. 6 (2017); René Repasi, “Legal Options for an Additional EMU Fiscal Capacity,” *Study for the European Parliament* PE 474.397 (2013). For economic discussions on the functions of a euro area budget, see Agnès Bénassy-Quéré, “Reconciling Risk Sharing with Market Discipline: A Constructive Approach to Euro Area Reform,” *CEPR Policy Insight* No. 91 (2018); Árpád Ábrahám et al., “On the Optimal Design of a Financial Stability Fund,” *ADEMU Working Paper Series* 2018/105 (2018). Also see the Draft Treaty on the Democratization of the Governance of the Euro Area (T-Dem), available at <http://tdem.eu/en/manifesto/>. Stéphanie Hennette et al., *Naar Een Democratischer Europa: Voorstel Voor Een Nieuw Verdrag* (De Bezige Bij, 2017). The T-Dem proposal is discussed in a special issue of *European Papers* (vol. 3, no. 1).

² European Commission, *The Five President’s Report: Completing Europe’s Economic and Monetary Union*, (2015). For an overview of the history of a Euro budget in the process of monetary integration, see Crowe, “Is a Separate Eurozone Budget a Good Idea?”; Pierre Schlosser, *Europe’s New Fiscal Union* (Palgrave Macmillan, 2019).

to MS to help them overcome an economic downturn and prevent small economic problems from turning into European catastrophes.

Whether the euro area budget will indeed fulfil the role of stabilizer is, however, not a foregone conclusion. The Four Presidents' Report from 2012 suggested another objective for a euro area budget, namely to promote structural reforms in the Member States.³ Financial support by the EU could facilitate the transition to new economic policies on the national level. Offering incentives for structural reforms would be complementary to another aspect of euro-crisis law, namely the extension of economic governance through the Six Pack and Two Pack. The purpose of the new budgetary tool subsequently became the focal point of the discussions. Whereas the support of structural reforms would imply the need for a budget of a very modest size, a stabilizing function would require a considerably larger budget. Folded into the discussion over the purpose are therefore the debates over how the budget is implemented and the size of the budget. Moreover, the function of the budget is also of relevance for the participation of non-euro area MS, or rather, for the ability of the euro area MS to *exclude* the non-euro area MS. Whilst there is clear wish for a specific budgetary instrument for the euro area, there are currently few legal arguments to exclude the non-euro area MS.

During the euro-crisis, one point of controversy was the prominent role of the MS in shaping the future of the euro, and an academic debate ensued over the new institutional balance in the EU.⁴ The negotiations for the new budgetary instrument can shed new light on these discussions in two ways; first, in showing where the center of gravity lies in negotiations over the future of the euro outside the crisis, and second, by creating new possibilities for EU institutions to grow their role in the management of the euro.

The ideas for the new budgetary function came together through a variety of sources. The Four and Five Presidents Reports set the agenda, followed by a set of initiatives from the Commission, including several proposals for legislation. The EP submitted its own ideas in 2017. The political debate was launched by the Meseberg Declaration by French President Macron and German Chancellor Merkel from June 2018. Opposition to an ambitious new budgetary function was organized through a loose alliance of several fiscally conservative (northern) MS, informally dubbed the New Hanseatic League. The resulting compromise for the BICC shows the balance of forces in the post-crisis euro era.

³ Herman Van Rompuy, 'Towards a Genuine Economic and Monetary Union', (December 2012).

⁴ Jürgen Habermas, *The Crisis of the European Union: A Response* (Polity Press, 2012).

As should be clear from this introduction, the debates over a euro area budget touch upon many different aspects of E(M)U constitutional law. This working paper first outlines several proposals that have appeared in recent years: the EP's resolution, the Commission proposals, the Franco-German Meseberg Declaration and the recent Eurogroup agreement. The comments will then focus on four constitutional aspects of the proposals: the legal basis, differentiation and purpose, the relation with the EU budget and the relation with the no-bailout clause.⁵ As will become clear in the following sections, the current proposals envision a new budgetary function with limited ambition (and thus of limited size). However, the history of EMU shows that where initiatives for reform are initially restricted due to political disagreement, there is a tendency for them to grow during a crisis. One question central to this working paper is whether the characteristics of the new BICC are such that they could enable the mechanism to quickly expand under different political circumstances, i.e. whether the BICC is a seedling that could grow into a full-blown Euro area budget.

2. Plans for a Euro (Area) budget

2.1. The Four and Five Presidents' reports

The Four Presidents' report from 2012 envisioned a fiscal capacity for EMU that would first offer financial incentives for Member States to adopt structural reforms on the basis of contractual arrangements. In a later stage, this would develop in a fiscal capacity that could facilitate adjustment to economic shocks through an insurance-mechanism.⁶

The Five Presidents' report from 2015 focused on the latter function, calling it a stabilization function for the euro area that would operate automatically. It expressly left the design of this function to an expert group, but defined its task in a negative sense. The stabilization function should not lead to permanent transfers, should not undermine the incentives for sound fiscal policy making and should not be an instrument for crisis management.

2.2. The European Parliament Resolution

⁵ For an overview of the reaction of economists to the BICC Term Sheet, see Inês Gonçalves Raposo, "The June Eurogroup Meeting: Reflections on BICC," *Bruegel Blog* (blog), June 24, 2019, <https://bruegel.org/2019/06/the-june-eurogroup-meeting-reflections-on-bicc/>.

⁶ Herman Van Rompuy, "Towards a Genuine Economic and Monetary Union, (December 2012), 9-12.

In February 2017, the European Parliament adopted a resolution on budgetary capacity for the euro area.⁷ Beyond the tasks of incentivizing structural reforms and addressing *asymmetric* shocks, the EP also envisioned the new capacity to address *symmetric* shocks that affect the euro area as a whole.

Instead of contractual arrangements for the encouragement of structural reforms, the resolution laid out a new ‘convergence code’, which would function beside the Stability and Growth Pact, and which would offer an ‘investment strategy’. It would focus on new convergence criteria, such as taxation, the labour market, social cohesion and good governance. Compliance with the convergence code would be a requirement for participation in the fiscal capacity.

Funding for the budgetary capacity would first come from the Member States as external assigned revenue and later through an amendment of the system of own resources.

2.3. The Commission proposals (2018)

The Five Presidents’ report had tasked the Commission with assessing progress and outlining further steps, which it did first with a Reflection Paper on the Deepening of EMU in 2017.⁸ This was followed by a set of legislative proposals in December 2017, on amongst others the integration of the European Stability Mechanism in the EU legal order and on a European Finance Minister. A communication on new budgetary instruments for the euro area was also included in this package.⁹ In May 2018, the Commission submitted two more legislative proposals on a reform support programme¹⁰ and a European Investment Stabilization Function¹¹ (EISF, not to be confused with the European Fund for Strategic Investment, EFSI, also known as the Juncker Fund, or the European Structural and Investment Funds, ESIF). The two legislative proposals from May 2018 are discussed below.

2.3.1. Reform Support Programme

⁷ European Parliament, Resolution of 16 February 2017 on budgetary capacity for the euro area (2015/2344(INI)), P8_TA(2017)0050.

⁸ European Commission, *Reflection paper on the deepening of the economic and monetary union*, (2017).

⁹ European Commission, *Communication from the Commission: Further steps towards completing Europe's Economic and Monetary union: a roadmap*, COM(2017) 821 final; European Commission, *Communication from the Commission: New Budgetary Instruments for a Stable Euro Area within The Union Framework*, COM(2017) 822 final.

¹⁰ European Commission, Proposal for a Regulation of the European Parliament and of the Council on the establishment of the Reform Support Programme, COM(2018) 391 final.

¹¹ European Commission, Proposal for a Regulation of the European Parliament and of the Council on the establishment of a European Investment Stabilisation Function, COM(2018) 387 final.

The proposal for a Reform Support Programme consists of three parts, of which one aspect clearly builds on earlier steps by the Commission in this area, namely the Structural Reform Support Service that was introduced in 2015. This service offers technical expertise to MS that want to implement structural reforms. The second element of the proposal is a new reform delivery tool, which would offer MS financial incentives to reach the targets of structural reforms, as outlined in a ‘reform commitment’ entered into by a MS with the Commission. Another new aspect of the proposal was to include a convergence facility, that would prepare non-euro area MS to join the Eurozone.

The legal basis of the proposal is article 175(3) Treaty on the Functioning of the EU (TFEU) on economic, social and territorial cohesion and article 197(2) TFEU on administrative capacity building. The Reform Support Programme would be part of the EU budget. It would be included in the Multiannual Financial Framework 2021-2027 and would be allocated 25bn euro, of which 22bn euro for the reform delivery tool.

In parallel to this, the Commission has sought to test the reform delivery tool, submitting a proposal to amend the current Common Provisions Regulation.¹² The European Parliament rejected the proposal.¹³

2.3.2. European Investment Stabilization Function

The second leg of the Commission’s proposal for a euro area budget within the EU budget was the European Investment Stabilization Function. The Reflection Paper from 2017 had considered three options for a stabilization function, namely investment protection, unemployment reinsurance¹⁴ and a “rainy day” fund. The December 2017 Communication on New Budgetary Instruments prioritized the investment protection as it “would allow for a swifter roll-out in comparison to the two other options”.¹⁵ In May 2018, the Commission produced a draft regulation for this stabilization function, based on article 175(3) TFEU on economic, social and territorial cohesion.

¹² European Commission, Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 as regards support to structural reforms in Member States, COM(2017) 826 final.

¹³ European Parliament, Legislative resolution of 24 October 2018, P8_TA(2018)0407.

¹⁴ See for legal considerations about such a mechanism: René Repasi, “Legal Options and Limits for the Establishment of a European Unemployment Benefit Scheme,” January 2017.

¹⁵ European Commission, *supra note 8*, 15.

Support under the EISF would come in two forms: first, a MS experiencing a large asymmetric shock would receive a loan in order to invest in support of objectives as defined under the Common Provisions Regulation and to maintain public investment. Whether a country is experiencing an asymmetric shock would be determined by the level of unemployment in a MS, compared to the previous year and to the average of the previous five years. Upon repayment of the loan or when the interest over the loan is due, the MS could receive a second form of support, namely an interest rate subsidy, covering 100% of the interest rate costs.

The size of the loan a MS could receive would be determined by a formula that weighs the eligible public investment and size of the asymmetric shock. The maximum of loans to the MS would be set at 30bn euro. Neither the loans, nor the interest rate subsidy, would directly impact the EU budget, as the Commission would be authorized to borrow the required amounts for the loans and a Stabilization Support Fund would provide the interest rate subsidy. That fund would be established on the basis of an intergovernmental agreement.

2.4. The Meseberg Declaration & the New Hanseatic League

Adopted in June 2018, after the start of a new term for Chancellor Merkel and the election of President Macron, the Franco-German Meseberg Declaration set forth a vision for deeper integration, with considerable attention for issues of EMU.¹⁶ The creation of a euro area budget, it stated, would promote competitiveness, convergence *and* stabilization. However, the explicit purpose of the budget would be competitiveness and convergence. An unemployment stabilization fund would be examined later.

A follow-up statement in December 2018 developed further the Franco-German vision of a euro area budget.¹⁷ Here, the aim of the budget is convergence and reform, achieved through the co-financing of investment. The new budget *could* thereby also fulfill a stabilizing function, it is mentioned, because economic downturns put pressure on public investments.

The ‘fiscal rules’ of the Eurozone would set negative eligibility criteria, but the budget would not explicitly be oriented towards the fulfillment of the goals of economic policy as formulated through the

¹⁶ Joint Franco-German declaration, *Meseberg Declaration: Renewing Europe’s promises of security and prosperity*, (June 2018), available at: <https://www.diplomatie.gouv.fr/en/country-files/germany/events/article/europe-franco-german-declaration-19-06-18>.

¹⁷ *Proposal on the architecture of a Eurozone Budget within the framework of the European Union*, available at <https://www.consilium.europa.eu/media/37011/proposal-on-the-architecture-of-a-eurozone-budget.pdf>. Also see Mehreen Khan, ‘Franco-German eurozone budget lets down Team Macron’, *Financial Times*, 19 November 2018.

European Semester, nor of the European Structural and Investments Funds. Instead, the Euro Summit would provide ‘strategic guidance’ for the budget, which the Eurogroup would operationalize. MS would submit proposals to implement the budget, reflecting the funding priorities, which the Commission would approve.

Opposition to an ambitious Euro area budget came from the newly created Hanseatic League, a loose alliance of several Northern MS. One of its first joint statements concerned the architecture of EMU.¹⁸ Regarding the new Multiannual Financial Framework (MFF), it noted that the EU budget could be better aligned to implement structural reforms. Targeted investments by the EU, under the cap of the MFF, could be complementary. After the agreement in the Eurogroup in December 2018 (see below), a statement of ‘joint language’ further discussed the views of the members on a budgetary instrument.¹⁹ Notable elements of the letter are that the budget is envisioned to fall under the expenditure and own resources ceilings of the EU and that access to funds is conditional upon respect for the rule of law. The envisioned size of the new instrument would moreover be significantly below what the Commission had envisioned for its reform delivery tool (i.e. below 22bn euro).

2.5. The Eurogroup agreements on the BICC

The Eurogroup reached a tentative agreement on a Eurozone budget in December 2018.²⁰ The two main conclusions of the Eurogroup, supported by the Euro Summit, were that no conclusion could be reached on the stabilization function of the new budget and that the proposal by France and Germany would be the starting point of the further discussions.

In June 2019, the Eurogroup then reached agreement on a ‘term sheet’ for the Budgetary Instrument for Convergence and Competitiveness (BICC).²¹ Its name indicates its limited ambition, but the instrument would not only incentivize reform, but also public investment.

¹⁸ ‘Finance ministers from Denmark, Estonia, Finland, Ireland, Latvia, Lithuania, the Netherlands and Sweden underline their shared views and values in the discussion on the architecture of the EMU’, March 2018, available at: <https://www.rahandusministeerium.ee/en/news/shared-views-and-values-architecture-emu>.

¹⁹ ‘Joint Language on Ownership and Financing of BICC’, April 2019, available at: <https://www.rijksoverheid.nl/documenten/kamerstukken/2019/04/30/joint-language-on-ownership-and-financing-of-bicc>.

²⁰ Eurogroup, Report to Leaders on EMU deepening, Council Press Release 738/18, December 2018, available at <https://www.consilium.europa.eu/en/press/press-releases/2018/12/04/eurogroup-report-to-leaders-on-emu-deepening/pdf>.

²¹ Eurogroup, ‘Term sheet on the Budgetary Instrument for Convergence and Competitiveness’, Council Press Release 466/19, June 2019, available at: <https://www.consilium.europa.eu/en/press/press-releases/2019/06/14/term-sheet-on-the-budgetary-instrument-for-convergence-and-competitiveness/pdf>.

The priorities of the budget would be reviewed yearly by the Euro summit and the Eurogroup through strategic guidance. MS should then submit their proposals for reform and investment on the basis of the strategic guidance. The Commission, in cooperation with the Eurogroup, would assess the proposals, on the basis of transparent criteria. One set of eligibility criteria would come from the Common Provisions Regulation, as its macroeconomic conditionality applies. This means that a MS would not be able to receive funds if it is subject to certain decisions under the Stability and Growth Pact and the Imbalances procedures.

For the governance framework ‘an additional act’ is envisioned, next to a legislative act based on the Treaties and a Commission proposal. The size of the instrument will be determined “in the context of the MFF”. The Euro area MS would participate in the new budgetary instrument, as well as any MS participating in the Exchange Rate Mechanism II that wishes to do so. For other non-euro area MS, appropriate arrangements should be defined, when the financial aspects of the BICC are arranged. That also highlights the lack of agreement on the method of funding in the Term Sheet. No decision was made as to whether to finance the BICC through EU own resources or through external assigned revenue.

2.6. The Commission proposal (2019)

In July 2019, the European Commission submitted a legislative proposal to the European Parliament and the Council for (a part of) the governance framework of the BICC.²² It is based on articles 136(1)(b) and 121(6) TFEU.

The proposal lays out one aspect of the governance of the BICC, namely the formulation of the strategic orientations for reform and investment for the euro area (as a whole) and of country specific guidance. These two aspects are directly linked to the European Semester, as the strategic orientations shall be part of the euro area recommendation and the country specific guidance shall be in conformity with the country specific *recommendations*. The country specific guidance shall then be used by the Member

The Euro Summit took note of the agreement of the Eurogroup and highlighted the need for ‘ensuring autonomy of decision of the Euro area Member States’. Euro Summit Statement of 21 June 2019, Council Press Release 492/19, available at: <https://www.consilium.europa.eu/en/press/press-releases/2019/06/21/statement-of-the-euro-summit-21-june-2019/pdf>.

²² European Commission, Proposal for a Regulation of the European Parliament and of the Council on a governance framework for the budgetary instrument for convergence and competitiveness for the euro area, COM(2019) 354 final, July 2019.

States for their reform and investment packages (to be regulated under another Regulation), that shall form the basis for the actual funding decisions.

Although the BICC is not primarily concerned with stabilization, the proposal by the Commission provides for the “modulation of national co-financing rates”, in case the Commission and the Council find that a MS is experiencing a severe economic downturn.

3. Legal aspects of the BICC

The following paragraphs highlight several legal aspects of the BICC. As the current plan is an amalgam of conclusions, informal agreements and proposals, my comments are tentative and will consider the overall direction in which the plans have developed.

3.1. The legal basis

The first issue concerns the legal basis for the budgetary instrument. The proposal submitted in July 2019 by the Commission is based on article 136 TFEU and article 121(6) TFEU but only concerns a part of the governance framework of the BICC. Another legislative proposal is expected that would create the BICC, most likely based on article 175(3) TFEU.²³ The Commission proposals for the investment stabilization and the Reform Support Programme, as well as the Franco-German proposal opted for article 175 paragraph 3 TFEU as legal basis, with the latter suggesting articles 182, 173 and 136 TFEU as possible supportive bases.²⁴

The Commission proposal for investment stabilization from 2018 provided a clear link between the objective of stabilization and the objective described by its legal basis, namely cohesion. Article 175(3) TFEU allows the Council and the EP to adopt measures to fulfill the goals of article 174 TFEU that cannot be achieved through the Structural Funds. These goals are territorial, economic and social cohesion, to the benefit of the harmonious development of the Union.²⁵ The main route through which these objectives are accomplished are the existing Structural Funds, which are regulated by, amongst other, the Common Provisions Regulation. As the Commission proposal connected the spending priorities of the new budgetary instrument for investment stabilization to the objectives as formulated through the Common Provisions Regulation, it is clear that the new instrument would be geared towards

²³ The reference here is to the third paragraph of article 175 TFEU.

²⁴ These legal bases concern industrial policy, research and technological development and the euro.

²⁵ Measures based on article 175(3) TFEU may aim at a specific form of cohesion. Repasi, “Legal Options and Limits for the Establishment of a European Unemployment Benefit Scheme,” 21.

the same objectives as the existing funds. As the objective of stabilization cannot be achieved through the existing funds, it is also clear that a new mechanism is needed, thus satisfying the two requirements of Article 175(3) TFEU.

The Commission proposal for the Reform Support Programme was also based on article 175(3) TFEU, in combination with 197(2) TFEU, but here the connection with the legal basis is more tenuous. Rather than connecting it directly to the CPR Regulation, the proposal sees cohesion as a result of “improving the national economies ... and social structures in the Member States”.²⁶ The Reform Delivery Tool is primarily oriented towards the objectives of the European Semester; cohesion is only a secondary objective. Hence, the suitability of article 175(3) TFEU as a legal basis is questionable. Using article 175(3) as the legal basis for the BICC is problematic for the same reason.

The main issue is whether convergence and competitiveness can be seen as stimulating a form of territorial, social or economic cohesion. One argument against equating convergence and cohesion is that the former arises from a legal field that has traditionally promoted market-based solutions for achieving Union goals, whilst the latter is more closely associated with public interventions to achieve those goals.²⁷ Rather than use cohesion policies to mitigate negative effects from market integration and the single currency, cohesion policies would now be defined in terms of market integration and monetary stability. National experiences with reforms associated with membership of the Eurozone are often defended in terms of economic necessity and efficiency, rather than cohesion. Perhaps the promotion of public investments is what brings the BICC closer to the original purpose of cohesion policies, but then the question is why the existing funds are insufficient to achieve this goal.

3.2. Differentiation and the purpose of the BICC

One of the points of discussion on the BICC is the relation between the Members of the Euro area and non-euro area MS. Naturally, the idea of a specific budget for the euro area would be contradicted by the inclusion of non-euro area MS. However, the debate over differentiation does not appear to be

²⁶ Article 4(a) of the proposal. It is furthermore noted in article 6 that the objectives shall refer to policy areas related to, amongst others, cohesion, competitiveness and productivity.

²⁷ It should be noted that the proposal for a new Common Provisions Regulation also aims to align the ESI-Funds with the goals of the European Semester. European Commission, Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument, COM(2018) 375 final. See e.g. articles 8(a), 9(1) and 14(1) of the Commission proposal.

primarily concerned with the participation of non-euro area MS in the budget. Rather, the debate over differentiation appears to be a proxy for several other issues, such as governance, purpose, and funding.

Both the Commission proposal for investment stabilization and the Franco-German proposal refer to the need for an objective justification for the exclusion of non-euro area MS from the application of the budget. The *economic* rationale for a specific euro area budget would be that Eurozone MS have lost some of their tools to absorb or counteract certain economic phenomena, such as asymmetric shocks. In an asymmetric shock, a single MS or a group of MS of the Eurozone experiences a sudden economic downturn. Since these MS are part of the Eurozone, they cannot use their monetary policy tools, including the exchange rate, to stimulate their economies. Monetary policy is instead defined by the ECB for the Eurozone as a whole and the exchange rate also follows the economic conditions of the Eurozone as a whole. Hence the need for a tool on the European level that responds *quickly* and *targets a subset of MS*.

None of the proposals, however, neatly follows this narrative. The Commission proposal for investment stabilization would be available only for euro area MS and those participating in ERMII. However, its activation requirements solely see to the economic situation in a specific MS. It is therefore possible that all Eurozone MS would qualify at the same time for support.²⁸ The mechanism is thus not specifically addressed to *asymmetric* shocks, but also to *symmetric* shocks.²⁹ It follows in this regard the resolution of the European Parliament, which explicitly called for the budgetary instrument to also target symmetric shocks.

An economic justification for such a tool is certainly available, but it would touch upon a broader set of beliefs about the functioning of EMU as a whole, and hence be more controversial. Whereas a symmetric shock affects all MS, it does not (necessarily) affect the relative economic strength of the Eurozone Member States in relation to each other. Hence, the ECB can adjust monetary conditions for the Eurozone as a whole, and the exchange rate would also respond to the economic situation of the Eurozone as a whole. Reasons to Europeanize the response to a symmetric shock would be the

²⁸ Another issue with the proposal by the Commission is that the form in which support is offered is inconsequential for euro area MS who have easy access to the financial markets and who currently borrow at negative or very low interest rates. The proposal would therefore be most beneficial for MS who are experiencing economic difficulties and who are losing trust from financial markets.

²⁹ The Commission follows here a proposal by several economists. See Bénassy-Quéré, “Reconciling Risk Sharing with Market Discipline: A Constructive Approach to Euro Area Reform,” 15.

insufficiency of current monetary tools³⁰ and the high levels of public debt in certain Member States, which might stand in the way of significant stimulus packages on the national level.³¹ Those who consider that the origins of these two problems lie with some MS' specific current economic policies would thus oppose the Europeanization of the solution.

The Franco-German Proposal and the envisaged BICC also do not correspond to the economic justification for the exclusion of non-euro area MS, because stabilization would not be the primary objective. Rather, both seek to promote competitiveness and convergence through structural reforms and investments. Hence, the economic justification for the BICC that MS have lost the tools to counter asymmetric shocks does not apply. The loss of monetary policy tools does not inhibit Eurozone MS from adopting structural reforms and making investments.³²

The necessity of the BICC can certainly be defended on other grounds, but none of these grounds justify the exclusion of non-euro area MS. It should be noted that the necessity of the BICC for the euro does not, by itself, justify the exclusion of non-euro area MS. This is because the euro is a policy of the Union, not just of the Eurozone. This is best illustrated by the need for convergence. Convergence has been at the heart of the debates on the process of monetary integration.³³ Whereas some saw monetary integration as a means for European economies to converge, others saw convergence as a requirement for monetary integration. The Maastricht Treaty set several convergence criteria, including on levels of inflation and government deficits. It is therefore clear that convergence is a crucial aspect of EMU. It is, however, not exclusively applicable to the Eurozone MS, as most non-euro area MS are under a legal obligation to try to join the Eurozone. Non-euro area MS can therefore have an interest in a budgetary mechanism that might help them fulfill the convergence criteria.

³⁰ See Marijn Van der Sluis, "Similar, Therefore Different: Judicial Review of Another Unconventional Monetary Policy in Weiss (C-493/17)," *Legal Issues of Economic Integration* 46, no. 3 (2019).

³¹ Giancarlo Corsetti et al., "Macroeconomic Stabilization, Monetary-Fiscal Interactions, and Europe's Monetary Union," *ADEMU Working Paper Series* WP 2016/058 (2016).

³² There is a (new) economic perspective, Modern Monetary Theory, that advocates the use of monetary policy for a broad range of economic and social goals. From this perspective, the Europeanization and strict mandate of monetary policy are obviously a restriction on the ability of national and European policy makers to invest in a broad range of economic policies.

³³ As regards the objective of competitiveness, the case for restricting participation is even weaker. Competitiveness is connected to various areas of EU law, with no indication that it should apply only to a subsection of MS. For example, according to article 3 TEU, the aim of the EU is to establish an internal market that promotes a highly competitive social market economy.

This interest of non-euro area MS in the new budgetary instrument is not negated by the unwillingness of some of them to try to join the Eurozone.³⁴ Non-euro area MS are subject to many aspects of economic governance and might even face adverse consequences of ignoring the prescriptions it produces. Although the imposition of fines *within* the procedures of economic governance is excluded for non-euro area MS, this does not mean that economic governance cannot have financial consequences. For example, when in 2012 the Council found that Hungary (a non-euro area MS) had not taken sufficient action to remedy its excessive deficit, this led to a suspension of commitments from the Cohesion Fund for Hungary.³⁵ Given that structural reforms and public investments can help a MS fulfill its obligations under the procedures of economic governance, it would be contrary to the goals of EMU to restrict the application of the BICC to euro area MS only.

The weak rationale for differentiation also translates into a legal problem. The application of rules of secondary law to a subset of MS must be based on primary law, with EMU as the leading example. Where the Treaties do not foresee differentiated integration, a group of MS can make use of enhanced cooperation (article 20 and articles 326-334 TFEU). In some cases, secondary legislation that is not directly based on a rule of primary law that envisions differentiated integration builds on a distinction introduced elsewhere in primary law. The Single Resolution Mechanism Regulation, for example, is based on article 114 TFEU (internal market), but applies only to Eurozone MS and MS where close cooperation has been established. Notwithstanding some other difficulties with this setup, the legality of the differentiation as such is not in doubt, given the many direct connections between the Single Resolution Mechanism and the ECB, whose acts do not apply to non-euro area MS (article 139(2)(e) TFEU).³⁶

The question is therefore whether the likely legal basis for the BICC, article 175(3) TFEU, tolerates (or provides for) differentiated integration in this case. The text of article 175(3) TFEU is silent on this issue, but the measure must promote the goals as found in article 174 TFEU. This means that the

³⁴ The Commission proposal for the Reform Support Programme has an interesting feature in this regard. Access to the Convergence Facility, which is only open to non-euro area MS, would be conditional on the MS taking “demonstrable steps towards joining the single currency within a given time-frame”. This includes “a formal letter from the government of the Member State concerned to the Commission stating its clear commitment to join the euro area within a reasonable and defined timeframe”. If adopted, this would be further evidence of the reversal of the membership policy of the Eurozone, whereby the legal obligation to join the Eurozone is no longer the primary tool to promote monetary integration. See Thomas Beukers and Marijn Van der Sluis, “The Variable Geometry of the Euro-Crisis: A Look at the Non-Euro Area Member States,” *EUI Working Paper Law 2015/33* (2015).

³⁵ Viorica Viță, “Conditionalities in Cohesion Policy,” *Research for REGI Committee - European Parliament* PE 617.498 (2018): 22.

³⁶ Steve Peers, “Trends in Differentiation of EU Law and Lessons for the Future” (European Parliament, 2015), 11.

cohesion must benefit the harmonious development of the Union. This does not mean that targeted measures are prohibited as such. In *Parliament v. Council*, the CJEU allowed a measure specific to the situation in Ireland and Northern-Ireland.³⁷ Measures contributing to economic cohesion in Ireland and Northern-Ireland were found to contribute to the peace process and thus to the overall development of the Union as a whole.

As no economic rationale requires the exclusion of non-euro area MS, it is doubtful that the BICC can be seen as promoting the cohesion for the harmonious benefit *of the Union*. Many of the Eurozone MS are amongst the most prosperous in the Union and many of those outside the Eurozone are amongst the most economically disadvantaged. An instrument that seeks to promote the competitiveness and convergence of Eurozone MS, to the exclusion of non-euro area MS, can therefore not be seen as promoting the economic or social cohesion (of the Union).³⁸

The legal problem would not be alleviated by integrating the BICC into the Commission's proposal for the reform support programme as a replacement for the reform delivery tool. In the current proposal by the Commission, the reform delivery tool would also be accessible to non-euro area MS, with the convergence facility as a specific tool designed to achieve another goal of EMU in relation to non-euro area MS. The convergence facility cannot compensate for any exclusion of non-euro area MS from the BICC. Even if the convergence facility would be redesigned to offer a similar level of benefits for non-euro area MS as the BICC would offer for Eurozone MS, it is doubtful the separation can withstand legal scrutiny, given the absence of a legally relevant reason for such a separation.

As noted elsewhere³⁹, the relation between the Eurozone's *in's* and *out's* has been inverted over time. Whilst first the emphasis lay on the euro as the currency of the Union, with specific exceptions for those temporarily on the outside, now the Eurozone is seen as requiring a special place within the Union. The introduction of article 136 TFEU in the Lisbon Treaty was the most obvious symbol of this transformation, as it allows the Euro area MS to adopt measures, rather than exclude non-euro area MS from participation. The transformation is incomplete, however, as the status of 'MS with a derogation'

³⁷ CJEU Case C-166/07, *European Parliament v. Council of the European Union*, EU:C:2009:499.

³⁸ If the BICC cannot be adopted under article 175(3) TFEU on the ground that it does not foster cohesion, it would then also follow that the BICC cannot be adopted through enhanced cooperation (article. 20 TEU and article. 326-334 TFEU), as one of the conditions of enhanced cooperation is that it would not undermine cohesion.

³⁹ Beukers and Van der Sluis, "The Variable Geometry of the Euro-Crisis: A Look at the Non-Euro Area Member States."

still dominates the overall setup of the euro. The problems for the BICC in terms of differentiation are thus the result of an incomplete transformation in the legal thinking on the place of the euro in the EU.

3.3. The BICC as part of the EU budget

According to the Term Sheet, the BICC will be part of the EU budget. This means, amongst other things, that the Commission has the (primary) responsibility for the execution of the budget (article 17 TEU) and that the Court of Auditors scrutinizes its implementation. For the governance of the BICC, i.e. the expenditure side, the Term Sheet envisioned an ‘additional act’, for which the Commission has already submitted a legislative proposal. Left open by the Term Sheet is how the BICC is to be funded, through own resources or through an external assigned revenue.

The use of external assigned revenue would avoid some complications, while raising others. External assigned revenue is used to finance specific items of expenditure and enables contributions to the EU budget from non-EU sources.⁴⁰ The funding would thus not come from an own resource of the EU, but from the MS as organized through a separate international agreement. First, this avoids the involvement of non-euro area MS in the funding of the BICC. The use of the European Financial Stability Mechanism (EFSM) for Greece in 2015 showed the sensitivity of using EU funds for the support of a Eurozone MS. In that case, it was agreed that if the EU budget were used to indemnify the EFSM for any losses, the non-euro area MS would be compensated by the Eurozone MS.⁴¹ If the BICC would be financed through the own resources of the EU, a similar construction would be needed to compensate non-euro area MS. This can also be phrased the other way around: if the BICC is to be funded through own resources, there arises another reason to abandon a strict idea of differentiation. The second benefit of the use of external assigned revenue would be that the size of the BICC can grow quickly, as its size is not capped by the MFF. In a next crisis, the Eurozone MS could easily increase their contributions.

One complication in that regard is that the use of external assigned revenue deepens the reliance on *national* contributions for the functioning of EMU. Rather than develop a budgetary instrument that provides for a European value, based on a source of funding derived from European activities, the BICC

⁴⁰ Article 21 Regulation 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending Regulations 1296/2013, 1301/2013, 1303/2013, 1304/2013, 1309/2013, 1316/2013, 223/2014, 283/2014, and Decision No 541/2014/EU and repealing Regulation 966/2012 (1) OJ L 193/2018.

⁴¹ Council Regulation 2015/1360 amending Regulation (EU) No 407/2010 establishing a European financial stabilisation mechanism, O.J. L 210/2015.

reinforces the position of the MS as the interlocutors for EU policies.⁴² It would be the MS who would fund the new instrument and who would be its recipients. Such a setup would emphasize the net beneficiaries and net contributors of the mechanisms. If the BICC would lead to significant re-distribution amongst MS, this would be criticized on the grounds that the new instrument should not be geared towards redistribution. The Five Presidents' Report was very clear in this regard. If the BICC would *not* lead to significant re-distribution and the MS would receive back what they put into the BICC, the question arises as to the added value of the BICC. A third option would be that the distribution key would react to the economic situation in the MS, but this appears to be precluded by the lack of an express stabilization function.

Another issue is the reliance on an international agreement for the organization of MS contributions.⁴³ It counters recent attempts by the Commission to 'repatriate' the ESM Treaty and the Fiscal Compact in the EU legal order. Although the downside of the use of international treaties outside the Union legal order is easily exaggerated, a long-term view on the development of the euro should favor a single integrated legal framework for reasons of simplicity and clarity.

For the allocation of funding, the term sheet suggests a complicated interaction between the Euro summit, the Eurogroup, the preparatory committees of the Eurogroup and the Commission. This part of the proposal is thus also premised on the exclusion of non-euro area MS. The Commission Proposal for the governance of the BICC only regulates the easy part of this difficult process, namely the formulation of objectives for the euro area as a whole and for individual MS. More problematic will be the decision making on the actual allocation of funding.

According to the term sheet, the guidance from the Euro Summit and the Eurogroup should result in 'transparent criteria', on the basis of which the Commission can assess the national plans for investment and reform. Whilst the responsibility for the implementation of the expenditure of the BICC will formally rest with the Commission, the preparatory committees of the Eurogroup and the Eurogroup

⁴² See Craig and Markakis, "EMU Reform"; Miguel Poiars Maduro, "A New Governance for the European Union and the Euro: Democracy and Justice," *RSCAS Policy Papers* 2012/11 (2012). Also see High Level Group on Own Resources, 'Future Financing of the EU', (December 2016).

⁴³ 'Editorial Comments: Tinkering with Economic and Monetary Union', 55, *COMMON MARKET LAW REVIEW*, (2018).

itself are also involved. It will be challenging to translate this construction into a legal proposal that respects the constitutional responsibility of the Commission for implementing the Union's budget.⁴⁴

The involvement of the Eurogroup in this stage of the process also risks ongoing political bickering over the BICC; where the Council is not able to agree on 'transparent criteria' or a clear strategy for the whole Euro area, MS may attempt to steer the use of the BICC also in the last stage. The continuous involvement of the MS thus takes away the incentive to formulate clear criteria. A clearer separation of responsibilities in the implementation of the BICC would be more likely to lead to clear priorities.

Notably absent from these arrangements is the EP. Whereas in part this logically follows from the close connection of the BICC to the European Semester, where it is also the Council that takes center stage, it goes against the movement to strengthen the democratic legitimacy of EMU through the involvement of the EP. Although the Commission's proposal for the governance of the BICC calls for an extension of the economic dialogue, where the President of the Council, the Commission and the President of the Eurogroup can be invited for discussion, it is doubtful this would lead to meaningful influence of the EP over the implementation of the BICC.⁴⁵ As budgetary matters are often seen as a core task of parliaments, it is unclear what justifies the exclusion of the EP in the formulation of priorities under the BICC.⁴⁶

3.4. The no-bailout clause

In other commentaries on euro-area reform, and also with regard to a euro area budget, article 125 TFEU (the so-called no-bailout clause) is sometimes discussed as a possible legal obstacle.⁴⁷ Article 125 TFEU is then seen as reflecting a principle of EU law with broad application.⁴⁸ It is argued here that this approach is mistaken.

⁴⁴ Since the Lisbon Treaty, the Commission is responsible for the implementation of the budget "in cooperation with the Member States". This reflected the fact that most Union funds are ultimately distributed by the Member States.

⁴⁵ Commission proposal on the governance framework.

⁴⁶ One contentious aspect of the involvement of the European Parliament in matters of EMU is the contribution of members elected in non-euro area MS.

⁴⁷ Lionello, "Establishing a Budgetary Capacity in the Eurozone. Recent Proposals and Legal Challenges," 833.

⁴⁸ Repasi, "Legal Options and Limits for the Establishment of a European Unemployment Benefit Scheme," 44.

Naturally, the interpretation by the CJEU of this provision in the *Pringle* case must be leading in any discussion on article 125 TFEU.⁴⁹ In *Pringle*, the Court set three requirements for the legality of financial assistance under article 125 TFEU: “1) Member States must remain responsible for their commitments to creditors, 2) the activation of financial assistance must be subject to strict conditionality and 3) this activation must be indispensable for the safeguarding of financial stability of the euro area as a whole.”⁵⁰ The discussion has focused so far on the three requirements and less on the *trigger* for these requirements: the provision of financial assistance.

The Court itself does not define what constitutes financial assistance, as there was very little reason to do so in the *Pringle* case. The ESM Treaty itself defines its support as financial assistance (article 3), and article 136(3) TFEU states that the granting of “any required financial assistance under the mechanism will be made subject to strict conditionality.” EU primary law furthermore speaks of financial assistance in article 122 TFEU, regarding EU support to a MS who is in difficulties or threatened with severe difficulties. Article 144 TFEU allows for mutual assistance, which is developed in Council Regulation 332/2002, creating a facility for medium term *financial assistance*. In these three instances, there is a direct connection between financial assistance and the existence of a crisis or difficulties in a MS. Hence, EU (primary) law offers no indication that financial assistance must be understood in a broad sense, but only covers emergency measures targeted at a single or a small group of Member States.

A restricted interpretation of financial assistance is also in line with the original purpose of article 125 TFEU, as it can be found in the proposals submitted by the MS in the negotiations leading up to the Maastricht Treaty. In their proposals, the MS put forward different versions of a no bailout clause, including a ‘*no automatic* bailout clause’ and a ‘*no unconditional* bailout clause’. The economic logic for a ‘no bailout clause’, which gained momentum throughout the negotiations, was that the growing interconnectedness between MS made them vulnerable to coercion by a MS in severe troubles.⁵¹ A single MS has leverage over its economic partners to demand economic support during a crisis, because an economic meltdown in one MS would spill-over into other MS. In ordinary times, when there is no immediate crisis, MS do not have this type of leverage over each other, leaving them free to decide together on projects that deepen integration or even promote outright solidarity on other grounds. In other words, what the no bailout clause sought to prevent was a form of forced solidarity in moments of

⁴⁹ CJEU Case C-370/12, *Pringle*, EU:C:2012:756.

⁵⁰ Bruno De Witte and Thomas Beukers, “The Court of Justice Approves the Creation of the European Stability Mechanism Outside the EU Legal Order: *Pringle*,” *Common Market Law Review* 50, no. 3 (2013): 838.

⁵¹ Marijn Van der Sluis, *In Law We Trust: The Role of EU Constitutional Law in European Monetary Integration* (European University Institute, 2017).

crisis. Since the BICC is not designed to assist MS in times of crisis and is available to all euro area MS, it must be concluded that the new budgetary instrument should, in its current form, not be considered to offer financial assistance. The requirements of article 125 TFEU are therefore not applicable.

A narrow approach to what constitutes financial assistance might also enable a strict interpretation of the requirements as formulated by the Court in *Pringle*. As the legality of many different proposal for further euro-reform are currently tested against article 125 TFEU, there is continuous pressure to interpret the three *Pringle*-requirements very narrowly, in order not to frustrate deepening integration. That pressure dissipates with a strict reading of ‘financial assistance’.

4. Conclusion

The negotiations over the BICC have been relatively straightforward, with a clear connection between the primary issue and the secondary issues. The primary issue is the overall purpose of the BICC, connected to that are the size, the method of funding, the governance structure and differentiated nature of the budget. The resulting compromise appears, so far, to be leaning towards those who favor a budget aimed at supporting reforms and national investments, implying a relatively small budget. The new budgetary instrument would be closely aligned with the objectives of the European Semester and part of the EU budget, but perhaps funded through external assigned revenue. This is the main issue still left undecided, although the exclusion of non-euro area MS appears to be a crucial step towards a decision to use external assigned revenue instead of own resources.

In the upcoming negotiations for the legal framework of the BICC and perhaps also in the implementation of the BICC, the debate will be over the balance between supporting reforms and stimulating public investment.⁵² Whereas the former is closely aligned with the needs of the European Semester, the latter invites the formulation of other European economic objectives and would thereby open the door to the further development of the BICC.

Both the process of negotiations and the substance of the agreements so far have centered on the MS. The agreements in the Eurogroup discarded the initiatives of the Commission in favor of an outline

⁵² In his remarks after the Eurogroup meeting of 13 September 2019, President of the Eurogroup Mário Centeno listed the following as remaining topics of negotiation: “Today we reviewed all the open issues under the BICC on the basis of work developed by the Commission during the break: the governance aspects, the financing, the allocation methodology, the modulation procedure and arrangements for the non-participating Member States.”

proposed by two Member States. The influence of the EP so far seems negligible; the question is to what extent it will be able to demand changes to a finalized political compromise between the MS.

What has been remarkable in the negotiations amongst the Member States so far was the two-step process through which the ambitious plans of the French have been scaled down. The first step was the negotiations with the Germany, in which the stabilization function was already demoted to a secondary objective. It then appears that the German negotiators allowed the members of the New Hanseatic League to challenge their joint declaration in the second step of the negotiations.

In the setup of the BICC, the MS again loom large. In the setup as currently envisioned, the MS set the priorities through the Euro summit/Eurogroup, maintain their presence at the stage of the assessment of national plans and perhaps solely decide the size of the BICC, if the funding is arranged as external assigned revenue. One effect of the predominance of the MS in the setup and functioning of the BICC is that it would allow for a rapid expansion of the instrument under the right political circumstances. At the same time, it is doubtful whether in the long-term the reliance on the MS for the functioning of EMU is sustainable, in lieu of relying on strong, democratic institutions on the European level.

An ESM Backstop Facility to the Single Resolution Board: The Difficult Marriage of an EU Mechanism and an Intergovernmental Institution

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1. A common backstop to the Single Resolution Fund

In 2014, the European Union (EU) legislature put in place a Single Resolution Mechanism (SRM) for the European banking sector as an element of its ‘Banking Union’.¹ The SRM creates a centralized system of funding of resolution measures by a Single Resolution Fund (SRF). A Single Resolution Board (SRB) is responsible for the functioning of the SRM. The SRB is a so-called regulatory agency of the Union.² While the SRF is to be primarily financed by *ex ante* contributions of the banking sector itself, the Regulation also envisages the possibility of “financial arrangements” for raising additional financial means if necessary.³ This covers a large panoply of possibilities. In particular, the SRB may contract loans from commercial providers, if that is appropriate to optimize the cost of funding (Reg. 806/2014, Article 73) and it shall contract additional “reserve” financial facilities, including from public bodies, to enhance its credibility and ensure resilience in case of crisis (Reg. 806/2014, Article 74). The rationale for this is set out in Reg. 806/2014, recital 107: essentially, the purpose is to have a so-called “backstop”. This is particularly important in a Banking Union that has a larger perimeter than the sovereigns do, as, contrary to a classical federal state, the Union budget cannot borrow from financial markets, and therefore is constraint in its capacity to backstop the banking system in times of crisis. Those financial means have to be repaid through contributions from the banking sector. From the very beginning, Finance Ministers had agreed on the necessity of a so-called ‘common backstop’ in favour of the SRF to facilitate its borrowings.⁴ While it was not clear back then what form this backstop would take, the idea was to increase the firepower of the SRF in case it were to prove to be too low to face a systemic crisis or the resolution of a key player.⁵ Member States were also explicit on the need to protect taxpayers’ money, no matter the final design of the tool. The backstop had to be fiscally neutral over the medium term, which entailed that the banking sector would be ultimately liable for funding the

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¹ Regulation (EU) No 806/2014 of 15 July 2014, OJ L225, 30.7.2014, p. 1.

² See, in general, on EU agencies, for example Marijn Chamon, *EU Agencies between Meroni and Romano or the Devil and the deep blue Sea*, *Common Market Law Review* 48: 1055–1075, 2011; Berthold Rittberger, Arndt Wonka (eds.), *Agency Governance in the EU*, TaylorFrancis, 2013.

³ Reg. 806/2014, Art. 73 and 74. See also recital 107.

⁴ See December 2013 ECOFIN and Eurogroup statement (<https://www.consilium.europa.eu/media/21899/20131218-srm-backstop-statement.pdf>).

⁵ Lucas Guttentber, *Looking for the silver bullet: a comprehensive guide to the debate on ESM reform* (Jacques Delors Institut – Berlin, 2017), p. 7.

backstop, even through contributions raised *ex post*. Member States gave themselves a period of maximum ten years to have a fully operational backstop in place.

In 2015, the Five Presidents' Report on completing Europe's Economic and Monetary Union called for the swift implementation of the backstop and suggested the intergovernmental European Stability Mechanism (ESM)⁶ as the possible provider of a credit line to the SRF.⁷

When the Commission proposed in December 2017 the establishment of a European Monetary Fund, through the integration of the ESM into the EU legal framework, its proposal provided *inter alia* for the establishment of a common backstop to be provided by the envisaged European Monetary Fund to the SRF.⁸ This attempt to avoid an intergovernmental architecture for the backstop would require unanimous approval by the Council after obtaining the consent of the European Parliament, given that the legal basis of the proposal is Article 352 TFEU. However, so far it has not received much attention from the Council. While the European Parliament adopted a Resolution on 14 March 2019 calling for the incorporation of the ESM into the EU legal framework as well as the introduction of the backstop,⁹ the Council has only discussed the legislative proposal once briefly in an ECOFIN Council.

Instead of picking up the Commission proposal, the Euro Summits of December 2017¹⁰, June 2018 and December 2018 pushed for an intergovernmental approach. At the Euro Summit meeting of 29 June 2018 Leaders agreed that “[t]he ESM will provide the common backstop to the SRF”.¹¹ In December 2018, Leaders confirmed their agreement on the creation of a common backstop from the ESM to the SRF, as part of a larger reform of the ESM, and mandated the Eurogroup to work on its implementation by reforming the ESM Treaty.¹² They agreed a term sheet and the terms of reference, which set the main characteristics of the instrument.¹³ The ESM common backstop would take the form of a revolving credit line and would be a last resort tool subject to the principle of fiscal neutrality in the medium term.

⁶ The ESM is an intergovernmental organization located in Luxembourg. It operates under public international law for all euro-area Member States. They ratified the intergovernmental treaty establishing the ESM on 27 September 2012. The ESM is a permanent firewall for the euro area, providing financial assistance for euro-area Member States in financial difficulty, with a maximum lending capacity of €700 billion.

⁷ “The Five Presidents' Report: Completing Europe's Economic and Monetary Union”, by: Jean-Claude Juncker in close cooperation with Donald Tusk, Jeroen Dijsselbloem, Mario Draghi and Martin Schulz, 22 June 2015, p. 11.

⁸ COM(2017) 827. Proposal for a Council Regulation on the establishment of the European Monetary Fund.

⁹ European Parliament resolution of 14 March 2019 on the proposal for a Council Regulation on the establishment of the European Monetary Fund.

¹⁰ See the input not prepared by President Tusk ahead of the meeting of 17 December 2018 (https://www.consilium.europa.eu/media/32095/en_leaders-agenda_eurosummit.pdf)

¹¹ See the statement of the Euro Summit meeting on 29 June 2018 (<https://www.consilium.europa.eu/media/35999/29-euro-summit-statement-en.pdf>)

¹² See the conclusions of the Euro Summit on 14 December 2018 (<https://www.consilium.europa.eu/en/meetings/euro-summit/2018/12/14/>)

¹³ See “Term Sheet on the European Stability Mechanism reform”, 4 December 2018 (https://www.consilium.europa.eu/media/37267/esm-term-sheet-041218_final_clean.pdf) and “Terms of reference of the common backstop to the Single Resolution Fund”, 4 December 2018 (https://www.consilium.europa.eu/media/37268/tor-backstop_041218_final_clean.pdf).

The euro-area Member States envisaged having the backstop operational by December 2023, which marks the end of the transition period given to the SRF to be fully mutualised and the ten-year period agreed when the SRM had been adopted. However, they did not exclude an early introduction of the backstop if there was sufficient progress by 2020 regarding risk reduction in the banking sector.

Initially, Leaders hoped to endorse the changes to the ESM Treaty by June 2019. Although there is still further work to be done, Member States reached an agreement of principle during the Eurogroup of June 2019 on the text of a revised ESM Treaty, which contains a brand new article 18A governing the backstop facility.¹⁴ A few days later, the Euro Summit of 21 June 2019 welcomed the progress made by the Eurogroup on the ESM reform and set December 2019 as new deadline for the delivery of the full package.

Therefore, while the details remain to be agreed, it is now clear that Member States have opted, at least for the time being, for a backstop to the SRF coming from the intergovernmental ESM. The legal basis of the backstop will be the ESM Treaty as amended, whose future Article 3(2) defines the provision of the backstop as an additional objective of the ESM.

This choice does not come without legal challenges. The EU and the ESM are closely linked, notably because of their partially parallel membership and objectives. What we have seen in the area of EMU is the emergence of what could be called a form of “semi-intergovernmental” method. It is intergovernmental in the sense that it takes place outside the institutional framework of the Union. At the same time a number of factors indicate a strong link and even interdependence with Union law.¹⁵ The EU institutions themselves are also closely involved in the functioning of the ESM. The Commission and the European Central Bank (ECB) negotiate with the recipient Member States the economic policy conditions linked to the ESM assistance. The Commission signs the Memorandum of Understanding on behalf of the ESM after it is approved by the latter’s Board of Governors. It is also the Commission who monitors its compliance. Members of the ESM Board of Governors are, *de facto*, the same individuals who are the members of the ECOFIN. Those individuals also meet informally as finance ministers of the euro area Member States in the Eurogroup. However, that interaction cannot hide the fact that the ESM is still an international organisation outside the EU legal framework.

Introducing a new ESM instrument whose recipient is an EU Agency entails close interactions with EU law. As seen during the design of the SRM, it is highly complex to tear apart the regulation of a mechanism and split it into issues governed by EU law and issues that follow the rules of

¹⁴ See the draft revised text of the treaty establishing the European Stability Mechanism as agreed by the Eurogroup on 14 June 2019 (<https://www.consilium.europa.eu/en/press/press-releases/2019/06/15/economic-and-monetary-union-eurogroup-agrees-term-sheet-on-euro-area-budgetary-instrument-and-revised-esm-treaty/>).

¹⁵ For a detailed analysis, see Jean-Paul Keppenne, «Institutional Report» in Ulla Neergaard and Catherine Jacqueson, Jen Hartg Danielsen (eds), *The Economic and Monetary Union: Constitutional and Institutional Aspects of the Economic Governance within the EU*, XXVI FIDE Congress (DJOF Publishing, 2014), 179, 203.

intergovernmental agreements between Member States (*inter se* agreements). Back then, Member States decided to leave the rules on the transfer and mutualisation of contributions to the SRF to an *inter se* agreement,¹⁶ which revealed the difficulty of combining both sets of rules.

In the rest of this paper, we briefly discuss some legal challenges that come out of this difficult marriage, first at the time of exchanging vows and, thereafter, during the shared life of the two partners.

2. Legal parameters for combining an *inter se* agreement with EU law

Agreements between EU Member States are not a novelty. Article 293 TEC, which has been repealed by the Treaty of Lisbon, provided for the conclusion of such *inter se* agreements in areas where the EU did not (yet) have competence, but which were deemed to be important for the proper functioning of the EU (in particular on the elimination of double taxation; recognition and enforcement of judgments and arbitral awards; and mutual recognition of companies). The Schengen agreement is another example of an *inter se* agreement.¹⁷

Some basic principles apply for combining those agreements with EU law. First, Member States may only enter into *inter se* agreements in areas where they retain competence.¹⁸ Second, the duty of loyal cooperation enshrined in Article 4(3) TEU obliges Member States to take due account of EU law when negotiating and concluding *inter se* international agreements.¹⁹ Finally, in case of conflict, EU law has primacy over *inter se* agreements.²⁰

The first principle protects the EU legal order when Member States negotiate *inter se* agreements. In *Pringle*, the Court applied to such *inter se* agreements the same standard as for international agreements with third countries, i.e. Article 3(2) TFEU.²¹ It stated that “*Member States are prohibited from concluding an agreement between themselves which might affect common rules or alter their scope*”.

¹⁶ Agreement of 14 May 2014 on the transfer and mutualisation of contributions to the single resolution fund (ST 8457 2014 INIT).

¹⁷ See on *inter se* agreements in more detail in particular: Allan Rosas, *The Status in EU Law of International Agreements Concluded by EU Member States*, 34 *Fordham International Law Journal* (2011), pp. 1304 to 1345; Angelos Dimopoulos, *Taming the Conclusion of Inter Se Agreements between EU Member States: The Role of the Duty of Loyalty*, 34 *Yearbook of European Law* (2015), pp. 286 to 318; Bruno De Witte, *Chameleonic Member States: Differentiation by Means of Partial and Parallel International Agreements*, in: Bruno de Witte, Dominik Hanf, and Ellen Vos (eds.), *The Many Faces of Differentiation in EU law*, intersentia 2001, pp. 232 to 267; Bruno De Witte, “*Old Flexibility*”: *International Agreements Between Member States of the EU*, in: Grainne de Burca and Joanne Scott, *Constitutional Change in the EU: From Uniformity to Flexibility*, Hart, 2000. See also, for a very critical view on *inter se* agreements, Julio Baquero Cruz, *What’s Left of the Law of Integration?* Oxford, 2018, pp. 169 to 198.

¹⁸ Case C-370/12, *Thomas Pringle v Government of Ireland*, EU:C:2012:756, paragraph 101.

¹⁹ See, by analogy to international agreements, Case C-620/16, *Commission v. Germany*, EU:C:2019:256, paragraph 93: “*It is essential to ensure close cooperation between the Member States and the EU institutions both in the process of negotiation and conclusion and in the fulfilment of the commitments entered into*”.

²⁰ Case 235/87, *Matteucci v Communauté française of Belgium*, EU:C:1988:460, paragraphs 19-23.

²¹ See fn. 15.

The Commission, in its role as guardian of the Treaties, can object whenever Member States try to negotiate an *inter se* agreement in an area where the Union has exclusive competence.

The second principle imposes certain duties on Member States when acting in the international sphere and these duties seem to apply *a fortiori* to agreements between Member States. In particular, the Court has addressed in several occasions the implications of the duty of loyal cooperation when the Commission has already submitted a proposal. For example, in C-246/07 *Commission v Sweden*, the Court stated that:

“Member States are subject to special duties of action and abstention in a situation in which the Commission has submitted to the Council proposals which, although they have not been adopted by the Council, represent the point of departure for concerted Community action”.²²

This finding could raise doubts as to whether Member States are entitled to negotiate through an intergovernmental structure a tool that is the subject of a pending legislative proposal. As mentioned above, Member States are currently negotiating their intergovernmental option while there is a pending legislative proposal from the Commission covering the same topic. In our view, this seems feasible only if Member States present their achievements as being (- if they ensure that those results in substance are indeed -) in line with the Commission’s proposal, thus merely as a first step before the future incorporation of the ESM into the EU legal framework.

In a way, this is what the Parliament did in its Resolution of 14 March 2019. While the Resolution recalls Parliament’s previous positions in favour of the incorporation of the ESM into the EU legal framework, it also states that *“in the short term, the ESM reform should contribute to the banking union, providing a proper common fiscal backstop for the Single Resolution Fund”*. Thus, the Parliament understands the reform of the ESM Treaty as a temporary solution, as a stepping-stone to achieving the ultimate goal of bringing the ESM into the EU legal framework. Similarly, the ESM and the Commission, in their joint position ‘on future cooperation between the European Commission and the European Stability Mechanism’, endorsed by the Euro Summit of December 2018, have set out: *“This note outlines joint proposals for the future cooperation between the two institutions in light of a further development of the ESM and taking into account the need to ensure full compliance with EU law as well as the longer-term goal of incorporating the ESM into the EU framework”* (emphasis added).²³

²² C-246/07 *Commission v Sweden*, EU:C:2010:203, paragraph 74. See also Case-804/79, *Commission v United Kingdom*, EU:C:1981:93, paragraph 28 and C-266/03, *Commission v Luxembourg*, EU:C:2005:341, paragraph 59.

²³ “Joint position of the European Commission and the European Stability Mechanism on their future cooperation ahead of the Euro Summit of 14 December 2018”, 14 November 2018 (<https://www.consilium.europa.eu/media/37324/20181203-eg-1b-20181115-esm-ec-cooperation.pdf>).

Finally, the principle of primacy protects the EU legal order both at the time of conclusion and during the life of the *inter se* agreement. First, when concluding *inter se* agreements, Member States need to comply with Union law.²⁴ Moreover, at the time of conclusion, not all eventualities are foreseeable. A treaty that is perfectly within the competence of the Member States may take on a life on its own (or an institution set up by that treaty may do so), and suddenly produce results that are contrary to EU law. Alternatively, EU law may evolve, and as a result an *inter se* agreement that was legal at the time of its conclusion is no longer so. In those situations, any provision that conflicts with EU law has to cede place to EU law, based on the principle of primacy.

In that context, it is also important to keep in mind that a provision of an *inter se* agreement or a decision of an institution established by an *inter se* agreement may very well fall within the competence of the Member States, but still violate a provision of EU law. In the field of double taxation treaties, that problem has arisen with regards to discrimination. In the field of the ESM treaty, it could arise where a decision of the ESM is not in line with the economic policy guidance of the EU. From the point of view of EU law, an international institution whose members are only EU Member States is nothing more than an emanation of these Member States. In other words, all the obligations entailed by the EU membership apply equally to this *inter se* institution.

We briefly present below a non-exhaustive list of areas where EU law and *inter se* agreements raises delicate legal questions.

3. Legal challenges of combining the two sets of rules

3.1. Safeguarding confidentiality

The Terms of Reference endorsed by the Euro Summit of December 2018 stipulated that the approval of disbursements by the ESM to the SRF should be made on a case-by-case basis by the ESM before the adoption of the resolution scheme. They also indicated that the ESM would decide “*on the basis of all relevant information while respecting mandatory legal confidentiality requirements*”.²⁵ This implies that the SRB would have to provide some information to the ESM to that effect. However, this exchange of information with the ESM might face some obstacles under EU law.

First, the members of the SRB are subject to professional secrecy under Article 339 TFUE and Articles 88 et seq. of the SRM Regulation.²⁶ They are in particular precluded from disclosing confidential

²⁴ See fn. 15: C-370/12 *Pringle v Ireland*, paragraph 69.

²⁵ See fn. 11: “Terms of reference of the common backstop to the Single Resolution Fund”.

²⁶ See fn. 1.

information received during the course of their professional activities, unless it is in the exercise of their functions, or when the information comes in a summarised or collective form such that individual entities cannot be identified, or when the authority or the entity which provided the information gave its express and prior consent. Moreover, such information cannot be disclosed to another public or private entity except where such disclosure is due for the purpose of legal proceedings. While it is true that Article 88(6) of the SRM Regulation allows for the flow of information between certain institutions potentially involved in the resolution process, including of the Member States, the ESM is not cited among them, despite the fact that it pre-dates the SRM Regulation, and the co-legislators were well aware of its existence and role.

Therefore, if Member States want to make the exchange of information possible without amending EU law, they need to find a way of overcoming these obstacles. One way could be avoiding sharing bank-specific information, so data would be provided in a summarised or collective form. Otherwise, one would need to opt for a broad interpretation of the relevant provisions. In that case, it could be argued that the SRB is executing its functions when exchanging information with the ESM and thus it finds its legal basis in Article 88(1). It also could be considered that the ESM falls within the scope of the Article 88(6), given that the composition of its Board of Governors comprises only national finance ministers, who are also part of the ECOFIN configuration of the Council, an institution with which the flow of information is allowed.

Second, some Member States may need, under their constitutional requirements, to share this information with their national parliaments. Such a step might interfere with the SRB's obligations under Article 88(4) of the SRM Regulation to ensure the safe handling and processing of confidential information, unless the necessary safeguards are in place at the level of national parliaments.

In addition, the question arises as to why the ESM, national governments and potentially parliaments would need that information. The clear risk is that they would start to second-guess the decisions proposed by the SRB for the resolution scheme. This raises important questions in relation with the autonomy of the EU legal order.

3.2. Safeguarding the autonomy of the EU legal order

Allowing in particular national parliaments to assess resolution decisions in advance would involve shifting their role from that of ex-post controllers, as foreseen in Articles 45 and 46 of the SRM Regulation and as is in general foreseen in national legal orders for the relationship between the executive branch and the legislative branch, to key decision makers in the crafting of the resolution decision. Such a role for national parliaments would undermine not only the decision to make banking resolution a task of the executive branch (SRB as regulatory agency; Commission as supervisor; and

Council, acting in its executive capacity, as final instance) but also the decision to confer on the EU the competence for banking resolution. The preparation of resolution schemes belongs to the SRB and is governed by EU law, irrespective of a backstop provided by the ESM. If the fear of a prospective negative decision from an ESM Member or its national parliament could influence the final design of the scheme, the principle of autonomy of EU law could be jeopardised.

This risk of undermining the autonomy of the EU legal framework is also present at a different level. The future ESM treaty foresees a provision on the so-called “permanence of the legal framework”. Under that rule, the backstop facility and its use are to be contingent upon the permanence of certain EU rules regarding bank resolution (or equivalent ones that lead at least to the same result).²⁷

The condition of permanence of legal framework risks undermining the ordinary legislative procedure under EU law. Indeed, if the Council decides with qualified majority, any Member State that has been outvoted and is member of the ESM could threaten to bring down the backstop to the SRF. That is a potent threat; hence, the Council is very likely to try to achieve unanimity on any decision that touches upon the permanence of the legal framework. Therefore, the condition of “permanence of the legal framework” could be seen as an undue interference into the autonomy of the EU legal order.

One last area where the autonomy of the EU legal order could be at stake is a possible interference of the ESM with the responsibility of the SRB for the functioning of the SRM. Indeed, one of the criteria for disbursements of the backstop credit line established in the Terms of Reference is observance of the principle of fiscal neutrality over the medium term. This means that the public money used for the backstop must be paid back in the medium term. For the ESM to be able to respect this principle, it would need to assess the repayment capacity of the SRF, which in turn entails an assessment of the repayment capacity of the banking sector. The ESM has a legitimate interest as a lender to carry out such an analysis. However, this assessment should not turn into a second-guessing of resolution decisions, which are the exclusive responsibility of the Union law bodies and are governed by EU law. In this regard, the legal provisions regulating how contributions are set are part of EU law. Therefore, if a body other than the one who is to make the final call interprets such rules, this could jeopardize the autonomy of the SRB to decide on resolution cases.

3.3. Ensuring accountability and legal responsibility

The ESM has no formal accountability to either the European Parliament, national parliaments or the Court of Auditors. Any accountability is indirect, through the control of national ministers of finance sitting as governors of the ESM by their national parliaments. Even though, as pointed out by the Court

²⁷ Article 18A(8) and 18A(9) of the draft revised text of the Treaty establishing the European Stability Mechanism. See fn 12.

of Auditors in Opinion 2/2018 concerning the proposal of the Commission to establish a European Monetary Fund, the Managing Director of the ESM appears before the European Parliament and the national parliaments when invited, the fact is that the ESM is essentially accountable to its Board of Governors.²⁸

By contrast, the SRB is accountable to the European Parliament, the Council, the Commission and the Court of Auditors, in accordance with Article 45 of the SRM Regulation. Therefore, if the ESM is to provide a credit line to the SRB for the use of the backstop, it might be envisaged to foresee a greater degree of accountability of the ESM. In that vein, the Parliament's Resolution on 14 March 2019 called for the establishment of a protocol for a Memorandum of Cooperation (MoC) between the ESM and Parliament to improve inter-institutional dialogue and enhance the ESM's transparency and accountability, notably through regular hearings, nomination rights and appropriate budgetary control rights. It also stressed that the Managing Director of the reformed ESM should be elected by and report to the European Parliament, following a proposal by the Council.²⁹

Moreover, the question can arise about the legal responsibility of the SRB for the actions committed while performing its backstop-related tasks.

Firstly, it is worth recalling that EU institutions may be liable before the Union courts for the actions they take in the roles that the ESM Treaty attributes to them. As the Court has already pointed out, the conduct of an EU institution is capable of incurring non-contractual liability on the part of the Union even when that conduct falls outside the EU legal order.³⁰ In particular, the Court found in *Ledra* that the Commission and the ECB must ensure that the memorandum of understanding that they adopt on behalf of the ESM complies fully with EU law.³¹ In *Bourdouvali*, the General Court was clear in extending such an obligation to the rests of the tasks conferred on them under the ESM Treaty, including their monitoring duties.³²

Secondly, the question of the legal responsibility of the SRB is especially relevant in the context of information-sharing with the ESM. If, as explained above, the SRB were to share information with the ESM for the purpose of the implementation of the backstop, there is a risk of engaging the non-contractual liability of the Union if such information eventually leaked. Therefore, the system must be

²⁸ Opinion No 2/2018 (pursuant to Article 287(4), TFEU) "The audit and accountability considerations concerning the proposal of 6 December 2017 for the establishment of a European Monetary Fund within the Union legal framework" (https://www.eca.europa.eu/Lists/ECADocuments/OP18_02/OP18_02_EN.pdf), p. 10.

²⁹ See fn. 8.

³⁰ Case T-786/14, *Bourdouvali and Others v Council and others*, EU:T:2018:487, paragraph 202, under appeal on certain points.

³¹ Joined Cases C-8/15 P to C-10/15 P, *Ledra Advertising v Commission and ECB*, EU:C:2016:701, paragraphs 55-60.

³² See fn. 27.

carefully designed so as to ensure that the Union is protected if the ESM fails to fulfil the confidentiality standards set under the EU legal framework.

4. Conclusion

As we have seen above, the choice that Member States have made to articulate the backstop to the SRF through an intergovernmental *inter se* agreement is not a straightforward, challenge-free, option. Marrying an EU mechanism and an intergovernmental institution requires developing legal solutions to the frictions created by combining both sets of rules.

However, at the end of the day, these legal challenges are no more than the result of a conflict between the legitimate interest of a lender and the principles of primacy and autonomy of EU law. Member States, as shareholders of the ESM, have a legitimate interest to make sure that the loan is given under sound conditions and will be repaid. However, the EU legal framework needs to protect itself from Member States circumventing the appropriate channels and agreements existent under EU law. It is there, in finding the right balance, where the real difficulty resides.

Greater convergence, more resilience? - Cohesion policy and the deepening of the Economic and Monetary Union

*Leo Flynn**

1. Introduction

Because the European Union has no inherent powers, any measure its institutions adopt must have a specific legal base that allows the Union both to act in the policy field covered by the act concerned and to act in the manner envisaged. In the economic policy field, those constraints are challenging. The hallmark of the Union's economic policy competences under Articles 121 and following of the Treaty on the Functioning of the European Union ('the Treaty' or 'TFEU') is that it is an activity of close coordination, based on a system of multilateral surveillance. There is a corresponding reliance on recommendations as the main legal instrument used, and while the Treaty sets out certain end-points in terms of fiscal performance (the well-known reference values of 3% of GDP for deficits and 60% of GDP for debt), they are aggregated targets that preserve great margin of choice for the individual Member States.

Those characteristics limit the possibility for the Union institutions to adopt measures that are binding as to how the Member States conduct their economic policies. The same features explain why the European Semester¹ constitutes the principal channel through which the Union institutions exercise their roles in the field of economic policy coordination.

However, when they wish to institute measures that will affect the economic performance of the Member States the Union institutions can take another route, to overcome the limitations associated with Article 121 TFEU. It is perfectly proper for them to adopt such measures on another legal base if the measures in question come within the ambit of the Treaty provision used. The fact that the effects of the measure will have an impact on economic policy does not mean that the use of that other legal base constitutes a circumvention of the limitations associated with Article 121 TFEU. The Court accepted in *Gauweiler* and *Weiss* that monetary policy measures taken by the European Central Bank ('ECB') do not fall into the sphere of economic policy for the sole reason that they may have indirect effects that can also be

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¹ The European Semester provides a framework for the coordination of economic policies across the European Union. It allows the Commission and the Council to discuss Member States' economic and budget plans and monitor progress at specific times throughout the year. The European Semester covers three blocks of economic policy coordination: structural reforms, focusing on promoting growth and employment in line with the Europe 2020 strategy; fiscal policies, in order to ensure sustainability of public finances in line with the Stability and Growth Pact; and prevention of excessive macroeconomic imbalances. The main "product" of the European Semester are the so-called country-specific recommendations ('CSRs'), based in part on Article 121 TFEU.

sought in the context of economic policy.² By the same logic, measures adopted by the other Union institutions under other policies are not equivalent to economic policy measures due to such indirect effects. Moreover, the fact that such effects are definitely foreseeable by the measure's author(s) and are knowingly accepted does not rob them of the status of 'indirect' effects.³

In recent years, the Union legislator has turned repeatedly to the cohesion policy chapter of the Treaty (Articles 175 to 178 TFEU) when considering such measures. It has done so, in large part, because the economic policy chapter of the TFEU allows for coordination measures but is relatively restrictive when it comes to the adoption of acts of a more 'binding' character. This paper seeks to provide a survey of those attempts, offering an overview of the initiatives taken and the legal issues they generate. It will start with a brief overview of the cohesion policy chapter, before turning to the existing legislation that affects economic policy in the Member States adopted under that Union competence, and finishing with an examination of the suite of pending legislative proposals.

2. An overview of the cohesion policy actions outside the Structural Funds

Article 174 TFEU introduces the concept of economic, social and territorial cohesion in the context of the Union (second paragraph), as well as referring to the specific types of areas and regions encompassed by that concept (third paragraph). The goal of cohesion policy is harmonious development of the Union, through a redistribution of (some of the) benefits resulting from the integration process embodied by the internal market and by economic and monetary union between the different parts of the Union.

Article 175 TFEU deals with the competences of the Member States and the Union in the execution of cohesion policy. Its first paragraph sets out the specific instruments available to the Union in order to attain the objectives of cohesion policy, chief amongst which are the Structural Funds ('the Funds') and the European Investment Bank. Its third paragraph provides a legal basis for the development of further specific action outside the Funds where such actions are necessary for strengthening cohesion. The Union institutions have turned to the third paragraph of Article 175 TFEU on a number of occasions, with increasing frequency over the past fifteen years.

The Solidarity Fund was the first instrument adopted under the third paragraph of Article 175 TFEU. Created originally in 2002, most of the rules governing the Solidarity Fund are in Regulation (EU) No 661/2014,⁴ which significantly adapts Regulation (EC) No 2012/2002. The Solidarity Fund operates

² Case C-62/14 *Gauweiler and others* EU:C:2015:400, paragraph 52; Case C-493/17 *Weiss and others* EU:C:2018:1000, paragraph 61.

³ Case C-493/17 *Weiss and others* EU:C:2018:1000, paragraph 62. For a critical commentary on that aspect of the Court's reasoning, see Van der Sluis, "Similar, therefore different: Judicial review of another unconventional monetary policy in *Weiss* (C-493/17)", (2019) 46 *Legal Issues of European Integration* 263, 272-273.

⁴ Regulation (EU) No 661/2014 of the European Parliament and of the Council of 15 May 2014 amending Council Regulation (EC) No 2012/2002 establishing the European Union Solidarity Fund, OJ L 159, 27.6.2014, p. 143.

with the Commission proposing to the Union budgetary authority that, in the event of a natural or man-made disaster of a sufficiently large scale, financial assistance will be made available to the national authorities to defray certain costs arising from the disaster.

In 2006, the Union turned again to the third paragraph of Article 175 TFEU, to create the European Globalisation Adjustment Fund ('EGAF').⁵ The EGAF acts, like the Solidarity Fund, as a re-financing mechanism. In other words, the beneficiary State undertakes and pays for operations it considers necessary to deal with the needs faced by its population, and later presents proof of payment and of the eligibility of those operations to the Commission. The latter reimburses the State up to the amount approved in the EGAF decision granting support.

The EGAF seeks to show the Union's solidarity with individuals in regions or Member States facing sudden and exceptional challenges in the labour market. Under it, the Union provides support to the Member State concerned, to assist workers made redundant because of major structural changes in world trade patterns due to globalisation and global financial and economic crises.⁶

Action based on the third paragraph of Article 175 TFEU is not limited to financial measures. In 2006, the co-legislators used that provision to adopt Regulation (EC) No 1082/2006, which allowed a new form of legal persons to be created, the European grouping of territorial cooperation (EGTC). EGTCs operate in more than one Member State and can consist of any of the following members: central, regional and local authorities of various Member States, bodies governed by public law and associations of any of those potential members who team up to deliver joint services which facilitate and promote cross-border, transnational and interregional cooperation.⁷

The Court has only had one opportunity to rule on the scope of the third paragraph of Article 175 TFEU, in the context of Case C-166/07 *Parliament v Council*,⁸ on the Union's financing of the International Fund for Ireland ('IFI'). The IFI is an international organisation established on foot of an international agreement between Ireland and the United Kingdom in the wake of the 1985 Anglo-Irish Agreement. It finances projects in Northern Ireland and the border counties of Ireland to promote peace and reconciliation. The Union had been the largest funder of the IFI since its creation, and by Regulation

⁵ Regulation (EC) No 1927/2006 of the European Parliament and of the Council of 20 December 2006 on establishing the European Globalisation Adjustment Fund, OJ L 406, 30.12.2006, p. 1. The EGAF is now governed by Regulation (EU) No 1309/2013 of the European Parliament and of the Council of 17 December 2013 on the European Globalisation Adjustment Fund (2014-2020) and repealing Regulation (EC) No 1927/2006, OJ L 347, 20.12.2013, p. 855.

⁶ The scope of the EGAF has been enlarged to cover economic disruption in the event of a withdrawal of the United Kingdom from the Union without an agreement: Regulation (EU) 2019/1796 of the European Parliament and of the Council of 24 October 2019 amending Regulation (EU) No 1309/2013 on the European Globalisation Adjustment Fund (2014-2020), OJ L 279I, 31.10.2019, p. 4.

⁷ Regulation (EC) No 1082/2006 of the European Parliament and of the Council of 5 July 2006 on a European grouping of territorial cooperation (EGTC), OJ L 210, 31.7.2006, p. 19.

⁸ Case C-166/07 *Parliament v Council* EU:C:2009:499.

(EC) No 1968/2006 it was to make a further financial contribution during the period from 2007 to 2010. The Council adopted the Regulation based on Article 308 EC (Article 352 TFEU), as it had done for all of the regulation's predecessors, despite the European Parliament arguing that the appropriate legal basis was the predecessor of what is now the third paragraph of Article 175 TFEU. When the Parliament challenged the validity of the IFI Regulation, the Court accepted that the Regulation's purpose was to support the actions of an international organisation established by two Member States, the objective of which is to strengthen economic and social cohesion. It noted that the objectives of economic and social cohesion under what is now Article 174 TFEU covered in particular economic and social improvement in the areas of Ireland where the IFI intervenes, as well as peace and reconciliation between the two communities in Northern Ireland. However, neither the arrangements governing cooperation between the Union and the IFI nor the conditions and method of payment in respect of the Union's financial contribution allowed the Union to prevent the use by the IFI of that contribution to cover actions which extended beyond the scope of the cohesion policy. For that reason, the Court found that the Regulation had to be based both on the third paragraph of Article 175 TFEU and on what is now Article 352 TFEU.⁹ The Court's ruling makes clear that while the material scope of the cohesion policy legal basis is broad, it is not infinitely elastic. As will be seen in looking at currently pending legislative proposals, the message taken from the IFI ruling focuses more on the opportunities provided by the third paragraph of Article 175 TFEU and less on its constraints.

3. Existing links between cohesion policy and economic policy coordination

The Union law acquis as it stands already contains links between the fields of cohesion policy and of economic coordination, with ties between actions in the former and the 'outputs' of the institutions in the latter.

3.1. 'Macro-conditionality' and the Funds

The most prominent of those links is the mechanism known as "macro-conditionality", under which the Member States' use of the Funds connects back to the various recommendations and decisions adopted in the field of economic policy coordination.¹⁰ Macro-conditionality rests on Article 23 of Regulation (EU) No 1303/2013,¹¹ which links the effectiveness of the Funds to sound economic governance.

⁹ A combination of legal bases that would not seem to be permissible post-Lisbon.

¹⁰ For a critical approach to macro-conditionality, see Bieber and Maiani, 'Enhancing Centralized Enforcement of EU Law: Pandora's Toolbox?' (2014) 51 Common Market Law Review 1057, 1081-1082.

¹¹ Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and

Under a so-called “first strand” of that macro-conditionality, the Commission may request the Member State concerned to re-programme the Union financing for its programmes to support the implementation of relevant Council recommendations made to it within the European Semester or under the excessive imbalance procedure.¹² Such a request must be reasoned and targeted, and cannot be made at the start or the end of the programming period for the Funds in question.¹³ A failure by the Member State to initiate re-programming in response to the Commission’s request can trigger a Council decision to suspend payments under the programmes or the parts of the programme identified in that request, until such time as the Member State takes steps for re-programming.¹⁴ There has never been a formal request under the first strand. Even so, the availability of such a tool creates incentives for the individual Member States to align their priorities, when they consider how to use the Funds during a given programming period, with the priorities of the Union institution as to how Member States should conduct their economic policies.

Under a so-called “second strand” of that macro-conditionality, the Commission must propose the suspension of commitments or of payments for the programmes of the Member State concerned. Those obligations arise if the Council takes two successive decisions indicating inadequate performance by a Member State in terms of the excessive imbalance procedure or finds a lack of effective action in an ongoing excessive deficit procedure. As a result, there is a tight link between the excessive deficit procedure and the excessive imbalance procedure, on the one hand, and availability of commitments and payments from the Funds on the other. Priority is given to suspension of commitments (which takes far longer to have an effect on the Member State), and indeed payments can only be suspended under the second strand where immediate action is sought and “*in the case of significant non-compliance*”.¹⁵

Unlike the first strand, the second strand of macro-conditionality is more than a theoretical backdrop, shaping the negotiating preferences of the Member States. In the previous programming period, of 2007-2013, the Council suspended commitments from the Cohesion Fund for Hungary after it had taken a decision under Article 126 TFEU establishing that the latter had not taken effective action to address its

laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006, OJ L 347, 20.12.2013, p. 320.

¹² Article 23(1)(a) and (b) of Regulation (EU) No 1303/2013. There is also a link with the various acts governing financial assistance programmes for Member States, which this paper does not consider.

¹³ Article 23(2) of Regulation (EU) No 1303/2013 provides that such a request cannot be made before 2015 or after 2019, a temporal limitation allowing Member States to advance in the implementation of their programmes. The well-known problems associated with starting the ‘pipeline’ of project execution under the programmes justify those constraints.

¹⁴ Paragraphs (6), (7) and (8) of Article 23 of Regulation (EU) No 1303/2013. The Commission has a period of three or four months (depending on whether or not the Member State responds to the Commission’s request with a proposal to amend the programmes) to propose to the Council that it suspend all or part of the payments for the programmes or priorities concerned. The Council decides on that Commission proposal by qualified majority vote.

¹⁵ Article 23(9) of Regulation (EU) No 1303/2013.

excessive deficit.¹⁶ The Council ended that suspension three months later, after the Commission found that Hungary had in the meantime taken effective action. In the present programming period, 2014-2020, after the Council decided in 2016 that Spain and Portugal had not taken effective action to address their excessive deficits, the Commission began moves to propose Council decisions suspending commitments for Structural Funds' programmes for both Member States. Ultimately, because the Council put their excessive deficit procedures into abeyance before the adoption of the suspension decisions, the Funds continued to flow in both countries. However, the prospect of such an interruption was disconcerting for those likely to be most affected,¹⁷ even though Article 23 of Regulation (EU) No 1303/2013 contains mechanisms to shield the most vulnerable final beneficiaries from the fallout of any such decisions.¹⁸

From a functional perspective, one can see that macro-conditionality mechanism provides a strong “push” for Member States to avoid outright rupture from the guidance that they receive within the economic policy coordination field. Nevertheless, in formal terms there is no sanction in operation here. The underlying logic of the mechanism is that only under conditions of sound economic governance can the spending under the Funds achieve their cohesion policy goals, and that economic mismanagement translates into a risk for the effective implementation of those goals.

3.2. The Structural Reform Support Programme

A second link between the fields of economic policy coordination and of cohesion policy is embodied in the Structural Reform Support Programme (SRSP). As part of the November 2015 European Semester package, the Commission proposed a regulation to establish the SRSP for the 2017-2020 period.

All participants in the multilateral economic surveillance process have identified structural reforms a priority area, to enhance growth and productivity and to address macroeconomic imbalances. The Commission proposal sought to address such needs, particularly in the areas of the regulatory environment for businesses, stimulating growth and increasing labour participation and productivity.¹⁹ The proposal drew on experience with technical assistance for reforms in Greece (the ‘Task Force for

¹⁶ Council Implementing Decision 2012/156/EU of 13 March 2012 suspending commitments from the Cohesion Fund for Hungary with effect from 1 January 2013, OJ L 78, 17.3.2012, p. 19.

¹⁷ See Answer given by Ms Thyssen on behalf of the Commission on 24 July 2017 to Question E-001685-17 “Implications of the possible freezing of EU funds for persons with disabilities”.

¹⁸ Annex III to Regulation (EU) No 1303/2013, on the scope and level of suspensions, foresees, for example, a reduction of the maximum level of suspension by 50% if the unemployment rate in the Member State concerned exceeds the average rate in the Union by more than eight percentage points. Annex III also provides that there should not be a suspension of programmes or priorities of critical importance to addressing adverse economic or social conditions. That latter category includes the Youth Employment Initiative as well as “[p]rogrammes or priorities [that] support investments related to the implementation of recommendations addressed to the Member State concerned in the framework of the European Semester and aimed at structural reforms”.

¹⁹ See Editorial Comments, ‘Tinkering with the Economic and Monetary Union’ (2018) 55 Common Market Law Review, 708, 713.

Greece’, established in 2011) and Cyprus (the ‘Support Group for Cyprus’, established in 2013), extending that model to all Member States, on a voluntary basis and at the Member State's request. The co-legislators adopted the Commission’s proposal in May 2017, as Regulation (EU) No 2017/825.²⁰

The SRSP offers technical assistance to all Member States, aimed at improving their institutional and administrative capacities for implementing structural reforms with a view to building strong economic foundations. It can offer national authorities technical support in a wide variety of policy areas, such as public financial management, administration, business environment, trade, competition, labour markets, education and training. The Commission organises support under the programme, but implements that support in cooperation with other Member States and international organisations (such as the OECD, the EBRD, the WHO and the UNHRC). Multiannual work programmes set out the SRSP’s policy objectives, expected results and funding priorities, while annual work programmes specify further details regarding implementation.

Under Regulation (EU) 2017/825, the SRSP received a financial envelope of EUR 142.8 million. Since the Commission’s proposal came midway through the 2014-2020 Multiannual Financial Framework, it put the financial envelope together from allocations under the Structural Funds. Various Member States and groups particularly concerned about the future dilution of cohesion policy-related spending successfully pushed to modify the proposal, by adding a recital noting that such a means of financing would not constitute a precedent.²¹ In addition, Regulation (EU) No 2017/825 allows Member States to make further contributions on a voluntary, including transferring of Structural Funds’ resources for technical assistance.

That initial financial envelope proved insufficient. Just over a year later, the co-legislators amended Regulation (EU) No 2017/825²² to increase the amounts available under the SRSP by EUR 80 million. At the same time, they modified the objectives of the SRSP to cover preparations by non-euro-area Member States to participate in the single currency.

Regulation (EU) No 2017/825 has a double legal basis, Article 197(2) TFEU²³ and the third paragraph of Article 175 TFEU. Since the objective of the SRSP goes beyond what Article 197 TFEU covers,

²⁰ Regulation (EU) 2017/825 of the European Parliament and of the Council of 17 May 2017 on the establishment of the Structural Reform Support Programme for the period 2017 to 2020 and amending Regulations (EU) No 1303/2013 and (EU) No 1305/2013, OJ L 129, 19.5.2017, p. 1.

²¹ Regulation (EU) No 2017/825, recital (17): “*The financing of the Programme through the transfer of allocations from [Commission] technical assistance [under the European Structural and Investment Funds] should only be considered a one-off solution that should not constitute a precedent as regards the funding of future initiatives*”.

²² Regulation (EU) 2018/1671 of the European Parliament and of the Council of 23 October 2018 amending Regulation (EU) 2017/825 to increase the financial envelope of the Structural Reform Support Programme and adapt its general objective, OJ L 284, 12.11.2018, p. 3.

²³ Article 197 TFEU is a legal base for Regulation (EU) 2015/825 due to the means by which the SRSP primarily acts (namely, by assisting national administrations in the implementation of Union law, in particular by means of inter-administration cooperation).

Regulation (EU) 2017/825 has a second legal basis, the third paragraph of Article 175 TFEU, allowing the SRSP to act outside the limits of Article 197(2) TFEU.

The rationale permitting use of Article 175 TFEU here is that actions undertaken to enhance the resilience of the economies of the Member States or to promote convergence between them can be considered as falling within the scope of cohesion policy where those actions strengthen the economic, social and territorial cohesion of the Union. Due to its potentially wide scope, that rationale has become a dominant theme in the set of cohesion-policy instruments proposed in 2018 and 2019 for whom the political narrative is that they strengthen the economic and monetary union.

In the handling of Member States' requests for support, Article 7 of Regulation (EU) No 2017/825 establishes two links with the European Semester. First, Article 7(2), dealing with the analysis of requests made by Member States, foresees that the Commission will carry out a dialogue with the Member State concerned in the context of the Semester when analysing the requests made under the SRSP. Second, Article 7(3), setting out the three categories of assistance that the SRSP may support, provides that requests for support may be made to implement “*growth-sustaining reforms in the context of the economic governance processes, in particular of the [CSRs] issued in the context of the European Semester [...]*”.

4. Greater reliance in the 2021-2027 period on cohesion policy instruments as a tool to strengthen EMU?

In light of the upcoming 2021-2027 Multiannual Financial Framework, the Commission tabled several legislative proposals for financial instruments to help strengthen the Economic and Monetary Union. Their legal basis is again the third paragraph of Article 175 TFEU, meaning that they are all specific actions to strengthen the cohesion of the Union outside the Funds. Their common justification as tools of cohesion policy is that completing reforms of a structural nature improves the performance of the national economies, thereby promoting resilient economic and social structures in the Member States. While there are evident links between such actions and economic policy, none of them uses Title VIII (‘Economic and Monetary Policy’) as a legal basis. Instead, they develop a concept of cohesion as embracing real convergence between the Member States and increasing their economies’ resilience.

4.1 The (initially proposed) Reform Support Programme

On 31 May 2018, as part of the suite of financial instruments for the post-2020 Multiannual Financial Framework period, the Commission proposed a Regulation on the establishment of the Reform Support

Programme ('the draft RSP Regulation').²⁴ The draft RSP Regulation envisaged a new financial instrument with, essentially, three parts; a technical support instrument to be the successor to the SRSP,²⁵ a so-called "Reform Delivery Tool", and finally a "Convergence Facility".

The Reform Delivery Tool ('RDT') was the major innovation in the draft RSP Regulation. It was to provide financial incentives for the implementation of reforms in Member States, with a financial envelope of EUR 22 billion. Unlike support from the Funds, financial contributions under the RDT would take the form of financing not linked to cost.²⁶ That approach recognises that addressing many of the Member States' structural challenges need more than investments or implementation of a programme; they may require a complex mix of policy actions and legislation, investments and improvements in governance of institutions and systems. It also encourages Member States to confront the high political costs in the short term associated with structural reforms, which can prevent or slow down their implementation or led to reversal of recently instituted reforms (often after a change in government) before they bear fruit.

In contrast to the SRSP, for which Member States can seek technical assistance for their own reform priorities as well as for those that the Council recommends to them in the context of the multilateral surveillance of economic policy, the RDT tightly linked reform proposals and the Semester. To be eligible for a financial contribution, reform proposals were to address effectively challenges identified in the context of the European Semester.²⁷ The greater the degree to which the reform proposal contributed to addressing those challenges, the higher the level of financial contribution the Commission could award to it.²⁸

Strong links to the Semester were also evident in other aspects of the draft RSP Regulation. Member States could submit their reform proposals to the Commission alongside their national reform programmes.²⁹ They could report on programme in achieving the reforms selected for support within the Semester process, and preferably in their national reform programmes.³⁰ There would be a role for the Economic Policy Committee in examining reform proposals, again maximising coherence with the Semester.

The Commission had intended to carry out a "test run" for the RDT, with a pilot phase for that programme. In its December 2017 package for deepening EMU, it proposed a Regulation that would allow Member States to use all or part of the performance reserve in the ESI Funds to support reforms

²⁴ Proposal for a Regulation of the European Parliament and of the Council on the establishment of the Reform Support Programme, COM/2018/391 final.

²⁵ Other than a significantly larger financial allocation (EUR 860 million), there are no major differences from the current SRSP.

²⁶ Article 15(1) of the draft RSP Regulation.

²⁷ Article 11(1) and (7) and Article 12(2) of the draft RSP Regulation.

²⁸ See Annex II to the draft RSP Regulation.

²⁹ Article 11(2) of the draft RSP Regulation.

³⁰ Article 14 of the draft RSP Regulation.

instead of specific projects ('the draft pilot phase RDT Regulation').³¹ The draft pilot phase RDT Regulation would have amended Regulation (EU) No 1303/2013, which lays down common provisions for the Funds, allowing Member States to use the funds transferred from the Funds' performance reserve to implement structural reforms identified in the Semester process. However, on 24 October 2018 the European Parliament rejected the Commission's proposal. That rejection reflected a political scruple, a fear on the part of supporters of more 'traditional' modes of delivering cohesion policy that allocating financial resources to action outside the Funds will ultimately be a zero-sum game, in which the Funds will emerge impoverished.

The last part of the draft RSP Regulation was to be a Convergence Facility, itself comprising two components. The first was a technical assistance component, and the second a financial support for reforms component ('the financial assistance component'). The difference between those two components and the other parts of the draft RSP Regulation was that they are dedicated to preparation for euro-area membership. They were to cater for the specific needs of non-euro-area Member States that embark on structural reforms, by offering additional tools for making their economies and social structures more resilient to shocks, better preparing them for euro-area membership. Support under the Convergence Facility would be open to non-euro-area Member States that had taken demonstrable steps to adopt the single currency within a given timeframe, thereby contributing to the fulfilment of the convergence criteria and to the resilience of the euro area as a whole. There would be a financial envelope of EUR 160 million for the technical assistance component and one of EUR 2 billion for its financial assistance component.

4.2. The Budgetary Investment for Convergence and Competitiveness

This paper describes both the RDT and the Convergence Facility in the past tense. It does so because, less than eighteen months after the Commission made its proposal, the political landscape has shifted completely due to the debates and political deals relating to what some describe as a "budget for the euro area".

The Commission had used a similar phrase in its December 2017 Communication, "New Budgetary Instruments for a Stable Euro Area within the Union Framework".³² President Juncker announced the Commission's intention to make concrete proposals for the creation of a "*dedicated euro area budget line within the EU budget*", providing for four functions. They were: (1) structural reform assistance, building on the Structural Reform Support Programme; (2) a stabilisation function; (3) a backstop for the Banking Union; and (4) a convergence instrument to give pre-accession assistance to Member States

³¹ Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 1303/2013 [...] as regards support to structural reforms in Member States, COM/2017/0826 final.

³² COM/2017/0822 final.

on their way to joining the euro. That move anticipated (or was built on) by France and Germany in their joint declaration of 19 June 2018 at Meseberg. The Meseberg Declaration proposed “*establishing a Eurozone budget within the framework of the European Union to promote competitiveness, convergence and stabilization in the euro area, starting in 2021*”.³³ While the Franco-German declaration did not endorse the notion of a stabilisation function, the two Member States also committed to “*examine the issue of a European Unemployment Stabilization Fund, for the case of severe economic crises, without transfers*”.

Those twin sources, from the Community method (in the December 2017 Communication) and the intergovernmental approach (in the Meseberg Declaration), came together in the conclusions of the Euro Summit of 14 December 2018. It mandated the Eurogroup to work on the design, implementation modalities and timing of a budgetary instrument for convergence and competitiveness (‘BICC’) of the euro area and ERM II Member States on a voluntary basis. The Euro Summit underlined that BICC would be part of the Union budget, coherent with other Union policies, subject to strategic guidance from euro-area Member States and be adopted on the basis of the relevant Commission proposal to be amended if necessary. That latter element said in a thinly disguised way that the May 2018 proposal for the draft RSP Regulation would be the vehicle for delivering the BICC.

The key features of the BICC as they emerged from the work of the Eurogroup³⁴ are that it should support both structural reforms and investment, going beyond the realm of structural reforms only (which is already a major difference from the RDT). Those structural reforms and public investment projects should reflect the strategic guidance on the use of the BICC provided by euro-area Member States, through the Eurosummit and the Eurogroup, and set out in the European Semester. The involvement of those bodies poses interesting institutional issues, but what stands out for the purposes of this paper is that it is clear that in discussions on the BICC no difficulties arise in carving out that new financial instrument from the RDT proposal, all the while retaining the same legal basis of the third paragraph of Article 175.

The BICC would cover euro-area Member States, and Member States in ERM II on a voluntary basis. That limitation to a subset of Member States is not necessarily legally problematic. To be permissible, the Union legislator will have to explain that the limitation is objectively justified in relation to the legal base used. In other words, it will have to identify shared factors amongst the Member States included, not possessed by the Member States who cannot participate, and set out why those factors are pertinent given the legal base of the BICC. The obvious common factor is the lack of any means to influence the exchange rate of the currency they use. Member States whose currency is the euro cannot respond to

³³The Meseberg Declaration is at: <https://www.diplomatie.gouv.fr/en/country-files/germany/events/article/europe-franco-german-declaration-19-06-18>.

³⁴ The Eurogroup Termsheet of 14 June 2019 on the BICC is at: <https://www.consilium.europa.eu/en/press/press-releases/2019/06/14/term-sheet-on-the-budgetary-instrument-for-convergence-and-competitiveness/>.

economic shocks by devaluing a national currency and so they possess fewer adaptation tools than are at the disposition of non-euro-area Member States. That shared characteristic is relevant in cohesion policy terms, because they are comparatively less flexible than the latter group and so are more exposed to having to reduce costs internally (with the consequent strains on wages, pensions and social spending) in the event of a major shock. For ERM II Member States, they are in a category of their own, with their currency linked to a central exchange rate against the euro but with some degree of flexibility. For that reason, it is probably legally defensible, in terms of the cohesion policy challenges addressed by the BICC, to foresee that they may participate but without making such a step obligatory.

That logic, of confining participation in a financial instrument aimed to address limitations resulting from a loss of exchange rate flexibility, was already present in another Commission proposal based on the third paragraph of Article 175 TFEU, for a European Stabilisation Investment Function ('ESIF'). Under the Commission's proposal of 31 May 2018,³⁵ the ESIF would, in the event of large asymmetric shocks, provide euro-area Member States with back-to-back loans of up to EUR 30 billion (guaranteed by the EU budget), coupled with a grant-like component to cover the full costs of the interest. The beneficiary Member State would have had to use those loans to maintain levels of public investment during the period of the downturn. At the time of writing, it seems unlikely that the ESIF Regulation will be adopted, hence the use of the past tense in describing the features of the proposed measure.

Nevertheless, the analysis in the Commission's explanatory memorandum for the ESIF gives similar (cohesion policy-relevant) reasons for proposing that instrument as justify basing the BICC on Article 175 TFEU:

As a result of the unification of monetary policy in a single currency area, macroeconomic policy instruments in the hands of participating Member States are no longer the same. While each country differs and the size and structure of the economy matter in terms of likelihood of being exposed to shocks, the crisis highlighted the limitations of means available to individual euro area Member States to absorb the impact of large asymmetric shocks.³⁶

4.3. A stronger link between the European Semester and Structural Funds

This paper already described the two strands of macro-conditionality by which, under the currently applicable legislation, the Structural Funds interact with the "outputs" from the European Semester process. For the next MFF, such links will be stronger.

Under the Commission's proposal for the successor Regulation laying down common provisions for the Structural Funds, the Member States should have regard to the recommendations they receive from the

³⁵ COM(2018) 387 final.

³⁶ COM(2018) 387 final, page 2.

Council in the European Semester when they are developing their programmes for 2021-2027. Because programming is a lengthy process, even though at the time of writing the legislative regime for 2021-2027 is still under discussion, the Council already “anticipated” the new rules when it adopted the CSRs in July 2019. Taking Belgium as an example, the Council included in the CSR to that Member State a so-called “investment recommendation”, while recital 22 explains that “[t]he programming of Union funds for the period 2021-2027 could help address some of the gaps identified in the recommendations”.³⁷

The Council was not alone in seeking to allow Member States to start their programming processes with guidance under the European Semester that anticipates the new legislative regime for the Funds. The 2019 CSRs also refer to Annex D to the “Country Reports” issued in February 2019. Country Reports are another “output” of the European Semester, but have a far lower legal status than CSRs. While the latter are only recommendations, the Council adopts them on a recommendation from the Commission, and it does so after the European Council has discussed them. By contrast, Country Reports are staff-working documents produced by the services of the Commission. However, by dint of the reference in the CSRs to a novel feature in the 2019 Country Reports (Annex D, setting out investment needs for individual Member States, with a strong territorial component), the Country Reports acquire a weight in the programming process they otherwise would lack. Their investment and territorial analysis underpins the investment-related CSRs proposed by the Commission and adopted by the Council in the 2019 Semester Spring package.

As a result, the Semester cycle of 2019 will guide the programming dialogue with Member States and regions on cohesion policy investments after 2020. The future cycles of the Semester will continue to take into account those reinforced links between investment needs and the use of the Funds. In particular, the 2024 Semester, which will coincide with the mid-term performance review of cohesion policy programmes, will provide investment guidance for the final two years of the next programming period.

5. Conclusion

The famously incomplete nature of the economic policy side of EMU has stayed in sharp focus ever since the outbreak of the sovereign debt crisis. The Union institutions have turned to a series of avenues by which they can address at least some of those gaps. It seems that, as a legal basis, cohesion policy offers a promising set of paths in that quest – even if in the late autumn of 2019 it is too early to be sure where those routes lead to, exactly.

³⁷ Council Recommendation of 9 July 2019 on the 2019 National Reform Programme of Belgium and delivering a Council opinion on the 2019 Stability Programme of Belgium, OJ C 301, 5.9.2019, p. 1. All of the Member States received an investment-related CSR in 2019 and for all except the United Kingdom there is a recital drawing their attention to the 2021-2027 programming exercise as a means to address those investment needs.

Moving beyond ‘institutional unity’ within the EU?

Euro area versus non-Euro area representation in the EU institutions

*Diane Fromage**

1. Introduction

When reflecting upon the future of the Economic and Monetary Union (EMU) for example, European Union (EU) institutions, and the European Commission especially, recurrently refer to its ‘unity’,¹ meaning that the ‘euro is the single currency of the EU’, and that ‘[w]ith the exception of the United Kingdom and Denmark, all non-euro Member States are legally committed to joining the euro eventually’.² This statement is undoubtedly in line with the European Treaties, as article 4-3 Treaty on the EU (TEU) unequivocally provides that ‘[t]he Union shall establish an economic and monetary union whose currency is the euro’. Yet, the question can legitimately be asked as to whether this provision really mirrors the current situation within the EU, i.e. whether it is still possible to turn a blind eye on the fact that the euro is unlikely to be adopted in the near future by all the seven Member States that should still legally adopt it.³ This is so both for political and for economic reasons. For instance, Sweden benefits from a *de facto* opt out regime and Poland made the conscious choice to stop making the reforms necessary to its adoption of the euro,⁴ while some other Member States are yet to fulfil the economic pre-requisites that would allow them to adopt the common currency.⁵

Against this background characterised by *de facto* permanent differentiation between euro area and non-euro area Member States (in the foreseeable future at least), a reflection as to how this reality should be mirrored in the EU’s institutional architecture should arguably be conducted. In other words, the question arises as to whether the principle of ‘institutional unity’ which has prevailed within the EU so far can continue to be upheld. Indeed, several euro area-specific informal bodies have arisen over the years – notably in the form of the Eurogroup (i.e. euro area ministers) and the Euro summit (i.e. heads

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¹ European Commission. Communication on Further steps towards completing Europe’s Economic and Monetary Union: a Roadmap COM(2017) 821 final, 2017.

² Ibid, 2-3.

³ These are: Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania and Sweden.

⁴ See further on the Polish case: A. Czerniak and A. Smolenska, ‘Poland without the euro. A cost benefit analysis’, *Polityka insight*, 2019.

⁵ In accordance with art. 140-1 Treaty on the Functioning of the EU (TFEU), ‘[a]t least once every two years, or at the request of a Member State with a derogation, the Commission and the European Central Bank shall report to the Council on the progress made by the Member States with a derogation in fulfilling their obligations regarding the achievement of economic and monetary union.’ For the latest of these convergence reports, see: European Commission, ‘Report from the Commission to the European Parliament and the Council. Convergence report 2018’, COM(2018) 370 final, 2018.

of States and government of euro area Member States).⁶ Over recent years, they have also recurrently met in ‘inclusive format’, i.e. with representatives from all EU Member States bar the United Kingdom (UK). They also exist next to the European Central Bank (ECB) which is an institution of the EU as a whole,⁷ and which operates within an EU28-wide European System of Central Banks (ESCB) but whose decisions only bind euro area Member States. The need to introduce some sort of euro area-specific parliamentary body is additionally recurrently brought to the fore, and several proposals – considered later in this paper – have already been made.

The principle of ‘institutional unity’ had been included in the Nice Treaty in the framework of the possibility for Member States to proceed with enhanced cooperation where not all of them wanted to move forward at the same pace.⁸ The express reference to this principle was deleted in the Lisbon Treaty, but the EU institutions appear to acknowledge its implicit existence up until today, with respect to the European Parliament at least since its quality as parliamentary assembly of the euro area for instance is never questioned by the European Commission.⁹ In fact, in the framework of the discussions on the Treaty of Amsterdam that took place under the auspices of the European Parliament, the German conservative party CDU/CSU reaffirmed as early as 1995 that ‘‘In view of the increasing diversity of the EU, further flexible arrangements may well be required in the future, but these should not undermine the single institutional framework [...] The European Parliament as a whole will be responsible for exercising control over those Union policies which are pursued by a limited number of Member States on a temporary basis’.¹⁰ The EU institutions defended similar views as well.¹¹

It should additionally be noted that a reflection on the need to create euro area-specific institutions appears to be all the more pressing as significant powers have been transferred to the EU level following the economic and financial crisis. For example, the control exercised at the EU level over Member States’ economic policies has become tighter, and EU institutions/bodies are now responsible for bank supervision and bank resolution in European Banking Union (EBU) Member States (ECB and Single Resolution Board, respectively). In addition to this broader exercise of power at the EU level, it should be noted that other reforms have intervened that have led to the institutional framework recently becoming even more complex, for at least three reasons. Firstly, the rules governing the EMU are not only enshrined in EU norms, but they are also complemented by rules contained in intergovernmental

⁶ It should be noted that there have been ‘attempts to progressively extend euro area-specific meeting of ministers (Euro group) to formations of the Council such as the Employment, Social Policy, Health and Consumer Affairs Council (EPSCO) or the Competitiveness Council’. A. de Gregorio Merino ‘The Banking Union in EU law: an EU institutional law perspective’ in G. lo Schiavo, *The European Banking Union and the role of Law*, Cheltenham, Edward Elgar, 2019, 29-48, 36-37.

⁷ Art. 13-1 TEU.

⁸ Art. 43 TEU (Nice).

⁹ Communication from the Commission. A blueprint for a deep and genuine economic and monetary Union Launching a European Debate. COM(2012) 777 final/2, 35.

¹⁰ Emphasis added. European Parliament Task force on the Intergovernmental conference, ‘n.4 Briefing on differentiated integration’, 29 May 1995, 5.

¹¹ Id.

Treaties: this is, for instance, the case of the Treaty on Stability, Coordination and Governance (TSCG) adopted in 2012 which formalised the Euro Summits and specifically spelt out the need to have an interparliamentary conference on the matters that it governs.¹² Secondly, resort has increasingly been made to Eurogroup and Euro Summit meeting configurations in ‘inclusive format’, i.e. those meetings have not only brought together the ministers and the Heads of states and governments of euro area Member States but have instead included the participation of representatives from all Member States bar the UK. The distinction between euro area and non-euro area has thus become increasingly blurred, and the rationale underlying the choice of one configuration or the other is arguably difficult to identify for an external observer. At the same time, it should be acknowledged that decisions made by euro area Member States will also affect non-euro area Member States,¹³ and that all Member States participate in the EMU. Thirdly, the EBU was created in 2013, and euro area Member States must belong to it. However, non-euro area Member States have the possibility to participate in it without having adopted the common currency, and this possibility required the design of original decision-making mechanisms. Moreover, new reforms of the EMU and the EBU are under discussion, and some of them could further affect the EU’s institutional landscape (this would, for instance, be the case if the proposal of a euro area minister/High representative materialised).¹⁴

Considering all these factors, this paper aims at examining whether it is still viable to maintain the existing institutional framework and whether, therefore, the principle of ‘institutional unity within the EU’ can still be maintained.

To answer these questions, this paper first examines the main features of the euro area’s specific institutional architecture (2). Then it considers how differentiation could and should be reconciled within the EU institutions (3). A final part concludes by spelling out what the pros and cons of a formalisation of the distinction between euro area and non-euro area Member States are, and by considering whether we should move beyond the principle of ‘institutional unity’ (5).

Providing an in-depth analysis of all the EU institutions that are most closely involved in the governance of the euro area, i.e. the Commission, the European Parliament, the ECB, the Court of Justice of the EU, the Council and the European Council, is an impossible endeavour in such a short paper. Having regard

¹² Art. 13 TSCG.

¹³ This has been regularly stressed by the UK for example and, in fact, D. Cameron had succeeded in obtaining the specific reference to the need to protect the interests of non-euro area Member States in its February 2016 New settlement for the UK. Letter by President Donald Tusk to the Members of the European Council on his proposal for a new settlement for the United Kingdom within the European Union, 2 February 2016.

¹⁴ See *inter alia* for a summary of the initiatives presented by under President Juncker’s Presidency: ‘Completing Europe’s Economic and Monetary Union. The Commission’s contribution to the Leaders’ agenda’, 2019, available at: https://ec.europa.eu/commission/sites/beta-political/files/further-steps-completing-emu_en.pdf Commission President elect von der Leyen’s mission letter to the Commissioner designate for Economy, P. Gentiloni, only includes a general reference to a ‘focus on the further deepening of the Economic and Monetary Union’ but it does not include any specific reference to a change of the institutional framework in place. U. von der Leyen, ‘Mission letter to Paolo Gentiloni, Commissioner designate for economy’, 2019, 4 available at: https://ec.europa.eu/commission/sites/beta-political/files/mission-letter-paolo-gentiloni_en.pdf.

to its unique status as an EU institution whose decisions only apply to euro area Member States, the ECB will not be considered here. An additional, yet relevant, issue which cannot be considered in this paper either is the co-existence of EU norms and intergovernmental treaties and the institutional complexity that derives from it. Indeed, as noted by the European Commission itself, this situation leads to the existence of certain accountability gaps. It also leads to the existence of parallel structures. For example, the ESM Treaty establishes a specific Board of Auditors¹⁵ which therefore exists next to the EU's Court of Auditors.

2. Euro area-specific institutional architecture: main features

The informal euro-area specific Eurogroup and Euro Summit exist next to the Council and the European Council respectively. The Eurogroup was established in 1998¹⁶ in response to the need for euro area-ministers to coordinate their national policies, and its existence was acknowledged in the Lisbon Treaty.¹⁷ The Euro Summit started to convene in 2008, and it was formally anchored in the TSCG in 2012. As mentioned in the introduction, both informal bodies have also met in inclusive format (i.e. EU-27 format) over the past years.¹⁸ In fact, since September 2018 all Eurogroup meetings have taken place either exclusively in inclusive format or alongside a second meeting in euro area-format.

Additionally, as mentioned in the introduction, some initiatives that only affect euro area Member States, or affect some and not all EU Member States, exist on the basis of intergovernmental treaties. This is the case of the European Stability Mechanism (ESM), and of the TSCG. Whereas only euro area Member States are party to the ESM, 25 Member States have ratified the TSCG, although not all of them are party to the whole treaty.¹⁹ It is noteworthy that these two treaties assign competences and tasks to both euro area-specific bodies/institution and EU-wide institutions. Indeed, the ESM Treaty has assigned a crucial role to the Commission and the ECB, and its main decision-making body, the Board of governors has the same composition as the Eurogroup; in fact, the President of the Eurogroup also acts as its Chair.²⁰ The Court of Justice has also been assigned jurisdiction over the disputes that may

¹⁵ Art. 30-1 ESM Treaty.

¹⁶ P. Craig and M. Markakis, 'The euro area, its regulation and impact on non-euro Member States' in *Research Handbook on the Law of the EU's Internal Market*, P. Koutrakos and J. Snell (Ed.), 2017, Cheltenham, Edward Elgar, 289.

¹⁷ Art. 137 TFEU and Protocol 14 annexed to the Treaties.

¹⁸ Between 2014 and 2019, 10 Euro Summit meetings took place, 3 of which were in inclusive format. Of the 79 Eurogroup meetings organised in the same time span, 19 were in inclusive format.

¹⁹ The Czech Republic, Croatia and the United Kingdom are not party to it.

²⁰ Art. 5 ESM Treaty. This article actually also foresees the possibility for the Board's members to alternatively elect a chairperson and a vice-chairperson from among its members, but the Board members have not made use of this possibility so far. The involvement of the Commission and the ECB in the functioning of the ESM was subject to judicial review by the Court of Justice of the EU in the *Pringle* case (Case C-370/12, *Thomas Pringle v. Government of Ireland, Ireland, The Attorney General*, Judgment of the Court of Justice (Full Court) of 27 November 2012) See on this case, Special section 'The ESM before the Court', *German Law Journal*, 2013, 14(1)

arise in the implementation of the ESM. In the framework of the TSCG too, certain tasks are attributed to the Commission, the ECB and the Court of Justice.

The Commission made several proposals in its December 2017 Package²¹ that would change this situation if they were adopted. They included: the creation of a European Finance Minister who would be the Commission Vice-President in charge of EMU matters and the President of the Eurogroup (he/she would also be the Chair of the ESM/European Monetary Fund (EMF))²² and the creation of an EMF. The negotiations that have been on-going since December 2017²³ point to the fact that the EMF will not be established in the form originally proposed by the Commission, i.e. the ESM will not be ‘communitarized’ but will continue to exist as a (reformed) intergovernmental treaty outside of the EU legal order. Likewise, the proposal to create a euro area High representative has not been met with much enthusiasm on the side of the Member States. Therefore, almost two years after the Commission made its proposals, no change in these domains can be expected. The role played by the Eurogroup within the EU has arguably become less visible and controversial than it was during the peak of the economic and financial crisis, and the need to improve the democratic legitimacy of its actions has consequently perhaps become less salient. Member States have also had to face other more urgent matters, such as the Brexit negotiations, and there may have been little appetite to start profound reforms in other areas, particularly because the inclusion of the ESM in the EU legal order proposed by the Commission would have led to a loss of powers for the Member States. Moreover, with the potential Brexit, the balance between euro area and non-euro area Member States would significantly shift, and non-euro area Member States would only produce 14,5% of the EU’s GDP.²⁴ Therefore, the difference between euro area Member States and the rest of the EU Member States would diminish.²⁵

3. How to accommodate differentiation within the EU institutions

and T. Beukers and B. de Witte, ‘The Court of Justice approves the creation of the European Stability Mechanism outside the EU legal order: Pringle’, *Common Market Law Review*, 2013, 50(3), 805-848.

²¹ Policy package on ‘Completing Europe’s Economic and Monetary Union’ presented by the Commission on 6 December 2017 available at: https://ec.europa.eu/info/publications/economy-finance/completing-europes-economic-and-monetary-union-policy-package_en ; This initiative built on the Five Presidents’ report presented in 2015: J.-Cl. Juncker et al., ‘Five Presidents report. Completing Europe’s Economic and Monetary Union’, 2015.

²² See, on this three-fold personality: D. Fromage, ‘A parliamentary assembly for the Eurozone’, ADEMU Working paper 2018/134, 2018, 9f. and N. Xanthoulis, ‘The Commission’s proposal for a European Minister of Economy and Finance: Institutional empowerment, constitutional tensions and the ministerial taboo, CERiM Online paper 7/2018, 2018.

²³ Time of writing is October 2019.

²⁴ EUObserver, ‘EU mulls post-Brexit balance of euro and non-eurozone states’, 15 December 2017.

²⁵ See further on this question of the relations between euro area and non-euro area Member States post-Brexit: P. Tokarski and S. Funk, ‘Non-euro Countries in the EU after Brexit’, SWP Comment no. 3, 2019.

Even if the role of the Eurogroup, and of Executives in the euro area-governance generally,²⁶ are much less the object of debates at present than they were a few years back, it is still worth considering how differentiation could and arguably should be accommodated within the EU's institutions because of the fact that not all Member States will join the euro area in the near future, and because of the important shortcomings that exist at present, for instance in terms of democratic accountability and legibility. The main institutions concerned – European Parliament, Court of Justice, Commission, European Council and Council – will be examined in turn in the following paragraphs.

The European Parliament is arguably the institution whose adaptation to the asymmetry existing between euro area and non-euro area Member States has been most debated. Indeed, as mentioned in the introduction, the proposals made with a view to establishing some sort of parliamentary assembly/forum of parliamentary representation for the euro area have been numerous. They have ranged from the possibility to create a euro area sub-committee within the EP ECON sub-committee²⁷ to the idea of creating a second chamber. Many of those proposals have not been very detailed however.²⁸ The most elaborate one is certainly the one made by S. Henette, T. Piketty, G. Sacriste and A. Vauchez.²⁹ These authors proposed the adoption of a treaty to democratize the euro area governance framework (T-Dem) by means of the creation of a second chamber composed of a maximum of 400 members, with those members being MPs (4/5) and MEPs (1/5). This proposal does not seem suitable for several reasons, first and foremost because the possibility to entrust non-EU institutions prerogatives reserved to EU institutions in the EU Treaties by means of the adoption of an intergovernmental treaty would not be legally feasible,³⁰ as it would also not be possible to amend existing legislation, such as the ESM Treaty, by adopting this T-Dem. The design of the proposed assembly is in my view not suitable either, among other reasons because of the mixed membership between MPs and MEPs it foresees. This would indeed be likely to reproduce the difficulties that have arisen in the framework of the Interparliamentary conference for Stability, Economic Coordination and Governance in the

²⁶ Indeed, also the empowerment of the European Council as a consequence of the economic crisis was the object of much discussion at the peak of the crisis. See for instance: S. Fabbrini, 'Intergovernmentalism and Its Limits: Assessing the European Union's Answer to the Euro Crisis', *Comparative Political Studies*, 2013, 1003-1029; for a balanced evaluation: R. Dehousse, 'Why has EU macroeconomic governance become more supranational?', *Journal of European Integration*, 2016, 617-631.

²⁷ More on this in D. Curtin and C. Fasone, 'Differentiated representation: is a flexible European Parliament desirable?' in *Between flexibility and disintegration. The trajectory of differentiation in the EU*, B. de Witte, A. Ott, E. Vos (ed.), Edward Elgar, Cheltenham, 2017, 118-145.

²⁸ I. Cooper, *A Separate Parliament for the Eurozone? Differentiated Representation, Brexit, and the Quandary of Exclusion*, in: « Parliamentary affairs », 2017, 655-672, 656.

²⁹ S. Henette, T. Piketty, G. Sacriste and A. Vauchez, 'Draft Treaty on the Democratization of the Governance of the Euro Area (T-Dem)' in *Ibid. How democratize Europe*, 2019, Cambridge, Harvard University Press, 63-86. See for a more detailed analysis of this proposal: D. Fromage, 'Il T-dem e la sua proposta di una Assamlea per l'Eurozona come punto di partita per una riflessione di base sulla democrazia nella governance dell'Eurozona', in *Parlamenti e democrazia in Europa tra integrazione differenziata e federalismi asimmetrici*, C. Fasone, N. Lupo and A. Vauchez (Ed.), forthcoming, Bologna, Il Mulino.

³⁰ B. de Witte, *Constitutional Challenges of the Enlargement: Is Further Enlargement Feasible without Constitutional Changes?*, European Parliament In-depth Analysis PE 608.872, 2019, 23.

European Union.³¹ In that framework, the differences in terms of views, competences or cohesion with MEPs being much more of a cohesive group than MPs who come together a few times per year and otherwise work in their capitals and operate under a national logical risk becoming visible and obstacles to the good functioning of the Parliamentary Assembly. Beyond this, MEPs' participation in the Assembly appears to be problematic, both because this would not take the difference between EU-wide and euro area-specific policies into account, and because MEPs are elected across the whole territory of the EU. There would therefore be a discrepancy between the participating MEPs' electoral basis and the territory upon which they are called to legislate. However, the possibility to establish a euro area-specific ECON sub-committee within the EP with the participation of MEPs from all Member States does not seem to be suitable to ensure adequate democratic accountability of euro area-specific decisions either. It would only amount to the creation of a more specialised ECON committee but would reproduce its shortcomings. At this point, the proposal to create a second chamber composed of delegated MPs does not appear to be promising either, among other reasons because it could not be established without any treaty change, and because it would need to be carefully crafted in order to be truly beneficial and not a mere redundant duplicate of the EP. The SECG interparliamentary conference mentioned previously may, in my view, only partially contribute to improve democratic legitimacy in the near future. As it currently stands, it is unlikely to allow for anything beyond an exchange of information and best practices among MPs and MEPS.³² It therefore appears that although the accountability gaps existing in the current euro area governance structure are arguably the issue that most urgently requires the adaptation of the institutional framework in place by means of the creation of a specific parliamentary structure, none of the proposals made to date appear to be fully suitable. Alternatives must therefore be sought, and an attempt at this is made in conclusion.

At the other end of the spectrum of the EU institutions most involved in the governance of the euro area stands the Court of Justice. Indeed, the Court appears to be the one least needing differentiation: as per article 19-3 TEU, its role is to rule on actions brought before it and to give preliminary rulings. The fulfilment of these tasks does not require that a specific 'euro area chamber' be created but rather demands expertise in the EU's legal system.

The European Council, the Council and the Commission are more complex cases.

The Commission is to 'promote the general interest of the Union [... , to] ensure the application of the Treaties [... and to] oversee the application of Union law under the control of the Court of Justice of

³¹ See also on these shortcomings: E. Griglio and N. Lupo, 'The conference on stability, economic coordination and governance: filling the gaps of parliamentary oversight in the EU', *Journal of European Integration*, 2018, 358-373.

³² See for more details on this conference: D. Fromage, 'A comparison of existing forums for interparliamentary cooperation in the EU and some lessons for the future', *Perspectives on federalism*, 2018, 1-27.

the European Union'.³³ It is an independent,³⁴ collegiate body.³⁵ Considering this EU-wide function of the Commission, so far no specific 'euro Commissioner' has been appointed. The Juncker Commission (2014-2019) counted with a Vice-president for the Euro and Social dialogue (V. Dombrovskis) who was, however, also in charge of Financial Stability, Financial Services and Capital Markets Union, thus dealing both with the euro and with other, EU-wide, policies. In the new von der Leyen Commission, the specific reference to the euro was abandoned, and issues related to the common currency could be dealt with by three different commissioners: V. Dombrovskis in charge of *An economy that works for people*, P. Gentiloni, commissioner for Economy, and the commissioner for Internal market, yet to be designated. Perhaps this absence of a specific euro area-commissioner is justified at this stage by the strong intertwinement between the monetary policy and other EU-wide policies as mentioned before. Furthermore, the upcoming Brexit will reduce this difference during the new Commission's term. This absence of differentiation within the Commission is also in line with the Commission's role as a guarantor of the EU's interest as a whole in other forms of differentiated integration within the EU: even where not all Member States participate in a policy area, the Commission is always involved, and actually has the power to decide upon the later participation of Member States that had decided not to be involved originally.³⁶ This notwithstanding, it may be necessary to create a specific euro area commissioner instead of having shared responsibilities as is the case at present should a euro area specific budget be introduced at some point.³⁷ Depending on the form that such a budgetary instrument would take i.e. especially whether the resources would directly stem from euro area-economies, it could indeed require the establishment of a euro area-specific governance structure composed of a euro area-Commissioner, a euro area-parliamentary body (potentially composed of delegates from national parliaments) and an institutionalised Eurogroup.

It should additionally be noted that despite the principle of collegiality applicable to the Commission, several proposals were made that would either endanger it or even go against it. As mentioned previously, in its December 2017 Package, the Commission for instance proposed the creation of a permanent High representative for the euro who would chair the Eurogroup and be the Commission vice-president in charge of EMU. Even if it would not create a specific euro-area Commissioner, this proposal could pose a threat to the principle of collegiality.³⁸ Besides this, the implementation of this proposal does not seem to be desirable *inter alia* because it would threaten the Commission's independence and upset the division of competences between the Commission and the Member States in the implementation of euro area-policies.

³³ Art. 17-1 TEU.

³⁴ Art. 17-3 TEU.

³⁵ Art. 17-6 b TEU.

³⁶ See Title III TFEU on Enhanced cooperation.

³⁷ See M. van der Sluis' paper in this paper collection for more details on the on-going discussions.

³⁸ M. Patrin, 'The legal nature of the principle of collegiality: A general principle of EU law?' CERiM Working paper 11/2018, 2018.

Contrary to the European Parliament and the Commission, the Council and the European Council are already, formally and informally, differentiated.

The European Council's euro area-specific configuration, the Euro Summit, is not recognised in the EU Treaties, but in the intergovernmental TSCG adopted in 2012. The legality of the amendment of the functioning of an EU institution, the European Council, by means of an international treaty concluded by some of the EU Member States only is doubtful,³⁹ but it is certainly true that nothing in the Lisbon Treaty prevents European Council members from deciding to meet in euro area-configuration only. Between 2014 and 2019, it met very irregularly since four meetings were convened in 2015 alone, but none took place between December 2015 and July 2017. This happened even though article 12-2 TSCG prescribes that Euro Summits must be convened at least twice a year. Understanding the rationale for the organisation of Euro Summits appears particularly difficult, especially when they take place in inclusive format: the explanatory capacity of the upcoming Brexit is limited since no clear pattern emerges in the resort to Euro summits in inclusive format. In other words, the organisation of Euro summits with all Member States bar the UK is not a systematic alternative to EU-wide European Council since, for instance, reforms of the EMU were debated in inclusive format in June and October 2018 but the discussions continued in euro area-format only in December 2018, even if the October meeting was a preparatory step to that meeting. It is furthermore interesting to note that the TSCG provides for the involvement of non-euro area signatories of that treaty,⁴⁰ but the inclusive format has brought together all EU-27 Member States in any case, i.e. Croatia and the Czech Republic were represented too despite not being party to the TSCG. The TSCG additionally establishes some mechanisms with a view to guaranteeing the democratic accountability of the Euro Summit: '[t]he President of the European Parliament may be invited to be heard [, and t]he President of the Euro Summit shall present a report to the European Parliament after each Euro Summit meeting'.⁴¹ The democratic accountability channels could still be improved, both because the European Parliament is not the best placed institution to ensure the democratic accountability of euro area-specific decisions for the reasons mentioned above, and because in practice they have not always been used. Whereas the ECB's President sometimes participated in meetings held in 2018 and 2019 for instance, no mention is made to similar participation of the European Parliament's President.⁴² This gap may, however, be compensated by the regular dialogue that exists between the European Council and the European Parliament where European Council meetings and Euro Summits are organised together.

³⁹ P. Craig, 'The Eurogroup: Legitimacy, Democratic Accountability and Decision-Making', Presentation prepared for the EP Joint ECON-AFCO hearing on Institutional aspects of the new rules on economic governance and the role of the Eurogroup held on 5 May 2015, 3f.

⁴⁰ Art. 12-3 TSCG.

⁴¹ Art. 12-5 TSCG.

⁴² European Council, 'Meetings', <https://www.consilium.europa.eu/en/meetings/calendar/?Category=meeting&Page=1&dateFrom=2014%2F01%2F01&dateTo=2020%2F10%2F28&filters=1733>.

Even if Eurogroup meetings are informal as well, they are much more institutionalised and are convened much more frequently than Euro Summits. They have existed since 1998, and the Lisbon Treaty formalised their existence for the first time, in the Treaty itself and in a specific protocol (no. 14) as noted above. Since May 2018, they have sometimes been convened in inclusive format, and since September 2018 this has always been the case. Such practice can probably be explained by the fact that in earlier years, the Eurogroup had to deal with numerous crisis-related issues, such as the rescue programmes of euro-area Member States in difficulty. Also, and this is certainly an argument in favour of a higher level of formalisation of the Eurogroup, these meetings escape the accountability and transparency requirements that apply to standard Council meetings, even if they play a key role in their preparation. For example, annotated meeting agendas and summaries of their discussions have only been made public since February 2016,⁴³ and no obligation exists for the President of the Eurogroup to appear before the European Parliament, even if it regularly does so in practice.⁴⁴ This situation led to the fear that non-euro area Member States would be confronted with decisions made previously by euro area-Member States meeting in the Eurogroup. This fear could have been further exacerbated by the fact that the Lisbon Treaty opened the possibility for decisions affecting euro area-Member States only to be adopted with only the votes of euro area-ministers meeting in the Council.⁴⁵ The Court of Justice has found that this would clearly be in breach of the Treaties though.⁴⁶ When taking place in inclusive format, Eurogroup meetings also provide an opportunity for EU Member States to discuss future proposals without the UK, and to do so in a freer and less transparent manner than if these discussions happened in the framework of Council meetings. Other additional issues of accountability arise in relation to the way in which the Eurogroup and the Euro Summit interact and cooperate together. The Eurogroup is indeed led to play a key role in the preparation of Euro Summit meetings, and in the implementation of the latter's decisions, particularly when those leave some leeway for interpretation.⁴⁷

If (and when) Brexit happens, it will be necessary to observe how practice evolves. The question can in any case be asked as to whether those Eurogroup meetings in inclusive format are in line with the relevant Treaty provisions. Article 137 TFEU refers to 'meetings between ministers of those Member States whose currency is the euro' and Article 1 Protocol 14 states that 'Ministers of the Member States

⁴³ Eurogroup, 16 February 2016 <https://www.consilium.europa.eu/en/meetings/eurogroup/2016/02/11/>. More on the accountability of the Eurogroup : B. Braun and M. Hübner, 'Vanishing Act : The Eurogroup's accountability', Transparency International EU, 2019.

⁴⁴ B. Braun and M. Hübner, 'Vanishing Act : The Eurogroup's accountability', Transparency International EU, 2019, 34f.

⁴⁵ Art. 136-2 TFEU.

⁴⁶ European Court of Justice, Case C-24/04, *Commission v Council*, para 81. Further on this point : R. Repasi, 'The role of the Eurogroup in the economic governance framework', Presentation prepared for the EP Joint ECON-AFCO hearing on Institutional aspects of the new rules on economic governance and the role of the Eurogroup held on 5 May 2015, 3.

⁴⁷ P. Craig and M. Markakis, 'The euro area, its regulation and impact on non-euro Member States' in *Research Handbook on the Law of the EU's Internal Market*, P. Koutrakos and J. Snell (Ed.), 2017, Cheltenham, Edward Elgar, 300.

whose currency is the euro shall meet informally'. Those meetings shall be taking place with the participation of the ECB and the Commission, but no mention is made to non-euro area Member States ministers. Differently from the Euro Summits in inclusive format, perhaps the Eurogroup meetings in inclusive format are more problematic. On the one hand, it is clear that the Eurogroup is meant to prepare for Euro Summit meetings and that, therefore, membership to both bodies should be identical. On the other hand, however, the Eurogroup finds its legal basis in the EU Treaties themselves, and it must meet to fulfil a specific function, i.e. to allow those Member States that have adopted the euro to coordinate their policies having an impact on the single currency. The parallel organisation of meetings in inclusive format is formally not covered by the existing Treaty provisions, and, most importantly, it also largely defeats the purpose of the existence of the Eurogroup. Therefore, Eurogroup meetings in standard format must arguably continue to be convened in any case (as it has admittedly happened so far), and the inclusive format should be reserved to cases that absolutely require cooperation among EU-27 Member States only. In sum, not only does it appear that the Eurogroup has become more powerful in the course of the economic and financial crisis than could have been anticipated originally,⁴⁸ but the systematic resort to the inclusive format actually increases the democratic accountability gap of EMU governance as a whole.

4. Conclusion: Should we move beyond 'institutional unity'?

As shown in the previous paragraphs, the situation as it exists today clearly is not satisfactory. Yet, a formalisation in the EU's institutional architecture of the differentiation between euro area and non-euro area Member States presents both advantages and disadvantages; they will both be examined in turn in the following paragraphs before the question whether we should move beyond 'institutional unity' is considered.

The main advantages of mirroring the differentiation between euro area and non-euro area Member States in the EU's institutional landscape are the following: avoidance of duplications (or at least improvements thereof) and better coherence; higher levels of transparency; and increased possibility to establish efficient mechanisms to ensure democratic legitimacy. Allowing for the creation of 'variable geometry' EU institutions would make the EU institutional framework fitter to face an ever-increasing diversity within its ever-expanding territory in the future.

Despite these clear arguments in favour of formalising existing euro area-specific institutions (and creating new ones), such an evolution also includes important drawbacks such as an increased complexity of the EU's institutional framework induced by the creation of yet other institutions; the

⁴⁸ See among many others on this empowerment: P. Craig and M. Markakis, 'The euro area, its regulation and impact on non-euro Member States' in *Research Handbook on the Law of the EU's Internal Market*, P. Koutrakos and J. Snell (Ed.), 2017, Cheltenham, Edward Elgar, 291.

creation of permanent institutions fitted to a situation which – formally at least – is meant to remain provisional; and the clear distinction this would create between decision-making procedures applicable to euro area-matters and euro-wide i.e. internal market-related matters. More generally, this raises the question of the limits in the level of differentiation that can be introduced within EU institutions without them being too fragmented to function properly.

It follows from the preceding analysis that the answer to the question whether we should move beyond ‘institutional unity’ within the EU by formalising or creating euro area-specific bodies is far from clear at this stage, especially in the context of Brexit and at a time when no reform of the Treaties is likely to happen in the near future.

As underlined previously, several shortcomings should nevertheless be remedied:

1. Eurogroup and Euro Summit meetings in inclusive format should only be convened when absolutely necessary;
2. Transparency and accountability standards should be strengthened both with regard to Euro Summit and to Eurogroup meetings;
3. Better-suited mechanisms to ensure democratic accountability should be established: the European Parliament alone can hardly be the only arena in charge of fulfilling this task, and the existing interparliamentary conference has numerous flaws. National parliaments should be more closely involved collectively, and such involvement should happen both with and without the participation of the European Parliament.

From a general perspective, ‘[m]onetary policy has always been the most internally differentiated policy area of the EU’,⁴⁹ and this does not seem likely to change in the near future. After having examined the specificities of the euro area-specific institutional architecture, and the arguments for and against its formalisation, the question arguably arises as to what these findings mean for the EU institutional structure more generally. In other words, should we move towards a ‘variable geometry’ institutional framework within the EU in other areas in which not all EU Member States participate or is the euro area a special case? Should the principle of ‘institutional unity’ be abandoned? It is argued here that the euro area is undoubtedly a policy area that differs greatly from the other initiatives of differentiated integration, both because of its long-lasting character and because of the consequences that the decisions made in its framework have for EU citizens (suffice it to think about the impact of the ECB monetary policy decisions or the consequences of the programmes designed by the Troika). Therefore, the mismatch between membership to the EU institutions making decisions, and the scope of territorial application of said decisions is probably less problematic in other policy fields than it is for the euro

⁴⁹ F. Schimmelfennig, D. Leuffen and B. Rittberger, ‘The European Union as a system of differentiated integration: interdependence, politicization and differentiation’, *Journal of European Public Policy*, 2015, 22(6), 764-782.

area. Additionally, some of those policy areas that relate to Justice and Home Affairs matters, are already governed by special decision-making procedures that leave more powers to the Member States. Beyond all this, the necessity to preserve some coherence across the whole EU must be duly considered as the decisions made have an impact on all Member States, even if they apply to some of them only; this argument speaks in favour of some form of involvement of EU-wide institutions in any case.⁵⁰ It remains however that the question of the institutional adaptation to differentiation will need to be seriously considered if the EU Member States continue to become more numerous, thereby increasing diversity even further and making it more likely to be (quasi-)permanent.

⁵⁰ This idea was presented by B. de Witte in reference to EU bodies other than institutions at the CERiM Conference ‘Beyond EU ‘Membership’? Current issues and future perspectives’ held on 23-24 May 2019.

The euro as an international currency – a critical assessment of the reinvigorated target for the euro

*Klaus Tuori**

1. Introduction

The discussion on the international role of the euro has regained some emphasis in recent times. The Commission has suggested making the international role of the euro a target for the euro area in a report labelled *Towards a stronger international role of the euro*.¹ This raises several questions that need to be addressed to understand the topic at hand. The international role of a currency does seem to fall squarely in either economic, constitutional or political fields, but has elements of all of them. In the euro area this means also that it does not have a clear institutional or political locus.

The present paper starts with a brief assessment of the economic rationales of the Commission Communication to promote a broader international use of the euro. In section 2, the paper turns to the constitutional questions such as the the division of responsibilities and competences regarding the international role of the euro. Can it be constructed as a Treaty objective or task? To whom should this task be assigned? This relates to the perspective of the European Central Bank as the issuer of the currency. What bearing does the international role of the euro have on the ECB's monetary policy responsibilities?

Section 3 takes an economic and practical perspective by focusing on the nature and causes of the international role of a currency. Is it rather an indicator of economic (and political) success than a suitable target as such? What kind of benefits and costs could an extensive international role of the euro entail? Finally, the paper concludes by applying the previous constitutional and economic discussion to the Commission Communication.

2. The Commission Communication - its rationales and proposals

Late 2018, the international role of the euro became a topic when the Commission published its Commission's communication: *Towards a stronger international role of the euro*. It was later discussed,

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¹ Communication from the Commission to the European Parliament, the European Council (EURO SUMMIT), the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions. *Towards a stronger international role of the euro*, Brussels, 5.12.2018 COM(2018) 796/4

inter alia, at the Euro Summit² and also in the Economic and Social Committee, and was followed by sector-specific consultations.³

Importantly, the Commission Communication included a long list of proposals, large and small, that it proposed to enhance the international role of the euro. The major proposals included “completing the Economic and Monetary Union, Banking Union and Capital Markets Union to deliver sustained growth and provide for enhanced resilience to adverse shocks.” It goes without saying that if these were to deliver steady growth without shocks, they should be pursued regardless of their impact on the international role of the euro. The more specific and more concrete suggestions foresaw the strengthening of the liquidity and the resilience of European market infrastructures, the promotion of a full range of trustworthy interest rate benchmarks and also a fully integrated instant payment system in the EU. In addition, European bodies and mechanisms were to be encouraged to increase their share in euro-denominated debt and economic diplomacy was to be engaged with global partners to promote the use of the euro in payments and as a reserve currency. Even more specific steps were suggested to increase the use of the euro in the key strategic sectors of energy, commodities and transport. While many of the proposals clearly have their merits, their link to the international role of the euro remained quite unclear or even weak.

However, as a critical first step, the Communication tried to list the potential benefits that could result from this increased international role of the common currency. The benefits can be briefly analyzed to see whether the international role of the euro could have some tangible benefits for the euro area economy (or society more broadly).⁴

The first benefit suggested by the Commission is the lower cost and lower risk of trading internationally, as trading in euro removes the exchange risk and other currency-related costs. The idea is that if international trade uses the euro as its currency, mainly instead of the US dollar, the euro area economic actors face lower risks. This is an intuitive benefit, but its significance is not elaborated upon by the Commission. In a way, it is an extension to the benefits arising from the increased intra-euro area trade, which has been studied to some extent. In particular, the early assumption that lower transaction costs would increase intra-euro area trade after the introduction of the euro turned out to be unsubstantiated. The relative share of the intra-euro area trade did not increase with the introduction of the euro nor has

² It was discussed as a Commission contribution to the European Council and the Euro Summit on 13-14 December 2018.

³ See, for example, Commission Staff Working document, Strengthening the International Role of the Euro Results of the Consultations, SWD(2019) 600 final. https://ec.europa.eu/info/business-economy-euro/euro-area/international-role-euro_en. See also a list of presentations in the public hearing before the European Economic and Social Committee on "Strengthening the international role of the euro: European and international perspectives". <https://www.eesc.europa.eu/en/agenda/our-events/events/strengthening-international-role-euro-european-and-international-perspectives/presentations>.

⁴ A similar approach was used by Konstantinos Efstathiou and Francesco Papadia in their Bruegel blog article ‘The international role of the euro.’ <https://bruegel.org/2018/12/the-international-role-of-the-euro>

there been compelling evidence that there was a significant reduction in transaction costs. In contrast, the introduction of the single market and particularly the period 1990-94 saw major increase in the intra-EU trade.⁵ It would thus appear that transaction costs related to the use of the common currency are small compared to other hindrances to trade.

Second, the Commission suggests that European households, businesses and Member States would face lower interest rates in their respective lending should the euro have a larger international presence. The document does not provide a rationale for this effect, but it can be assumed that a more important international role would also create more demand for euro-denominated debt instruments and that the markets for euro-denominated instruments would be more liquid and deeper. This could be related to another benefit mentioned by the Commission, namely more reliable access to finance for European businesses and governments, even in periods of external financial instability. The problem with this claim is that it is not based on any substantial argumentation. Its potential flaws can be numerous. Taking the current situation as the starting point, it is difficult to see how the level of interest rates or the access to finance could be a problem. Up to now and also going forward, both the level of interest rates and the access to finance depend on a number of factors most of which are unrelated to the international role of the euro. While Efstathiou and Papadia see a major benefit arising from an increased financial autonomy of the euro area, it is also possible to envisage that a more profound role of the euro would lead to increased financial flows from and to the euro area that could also have adverse effects.

The Communication also sees as a potential advantage of a reinforced international role of the euro the “stronger autonomy of European consumers, allowing them to pay or receive payments for their international trade, and finance themselves with reduced exposure to legal actions taken by third country jurisdictions, like extraterritorial sanctions”. How the international role of the euro would bring about these benefits is somewhat unclear, as the currency of a contract and the jurisdiction of the contract are hardly related. It is, however, conceivable that particularly the US has used the international role of the dollar and particularly the dominant position in the international payment system of the key US banks as a means to put pressure on some countries. Whether the euro area countries have been subjected or are likely to be subjected to such pressures and would be protected from it by a stronger international role of the euro could be the rationale behind this claim.

Perhaps the most problematic claim in the Communication is that the international role of the euro would result in the “improved resilience of the international financial system and economy, less vulnerable to exchange rate shocks”. The scenario that the global economy would be less dominated by the US dollar, balanced by the role of the euro or by the euro and some other currency such as the Chinese renminbi, would be polarized. This polarization could actually increase the fluctuations between the pillars,

⁵ Rogers, John H. (2003). -Monetary Union, Price Level Convergence, and Inflation: How Close is Europe to the United States?’ working paper, International Finance Division, Board of Governors of the Federal Reserve System.

making the system less stable. The evidence is naturally scarce, but the passage from the UK sterling-dominated global currency system to the one dominated by the US dollar was hardly a smooth or a stable development.

Quite correctly, the Communication points out that a wider use of an international currency comes with increased global responsibilities. What these responsibilities include and who should take the decision to carry them out, is not discussed. Taking the example of Germany from the 1970s until the introduction of the euro shows how the balancing between domestic responsibilities and externally-imposed responsibilities can collide, perhaps to the detriment of the former or the latter. This could be discussed somewhat more with the constitutional assessment of the international role of the euro.

In conclusion, it is not very clear that there are tangible economic benefits arising from a more prominent international role of the euro, or that these benefits would outweigh the costs and risks involved. This leads to assume that the Commission's new emphasis on the international role serves some purposes other than the economic benefits for the euro area economy. For one, it is possible that the Commission has more of a strategic target by focusing on something that can be described as positive for the euro area as a whole. Arguably, the developments in the global economy have seen a turn towards more confrontational approaches across the Pacific Ocean. In this context, the strategic goal could be to stress the euro area perspective in the more competitive and political global economy. It can be a way to seek internal unity.

A somewhat different strategic aim would be to gain support for the reform agenda for the Economic and Monetary Union. Indeed, the agenda suggested by the Commission is not very closely related to the international role of the euro. Particularly, the main aim of the reform i.e. "Completing the Economic and Monetary Union, the Capital Markets Union and the Banking Union" is a very general one that includes the whole list of proposals that have been rationalized by different arguments before and partly implemented with limited success.

3. The constitutional perspective on the international role of the euro – whose decision and responsibility

The constitutional issues related to the international role of the euro could be approached in different ways. I will start with some remarks on the pre-history of the common currency that could provide some motivations for the international perspective. The bulk of the assessment, however, will focus on the relevant Treaty provisions to assess what kind of a Treaty task the international role of the euro could be and who, if anyone, should bear the main responsibility for advancing it.

It can be claimed that the euro has a background as a counterweight for the US Dollar. The 1960s already witnessed a growing dissatisfaction towards the dominant role of the US Dollar in the international

monetary order (the Bretton Woods system). The US was not seen to provide the stability that was demanded from the anchor of the international monetary system, which was particularly problematic for countries such as Germany that aimed at internal price stability. More generally, the structure where the European currencies were more linked to the US Dollar than to each other was unsatisfactory, particularly when other countries had to adjust to the impulses and shocks emanating from the US. The European response was to start planning for a common currency that found its first concrete proposal in the form of the Werner Report in October 1970.⁶

Although the plan contained in the Werner Report did not lead to much, the dissatisfaction with the US Dollar remained even with the collapse of the Bretton Woods, effectively in 1971 and formally in 1973. The US Dollar maintained its leading status. The German D-Mark was able to take a stronger position particularly in Europe, which became more formalized with the introduction of the European Monetary System (EMS) in 1979. In the system which was mainly based on the cooperation between the central banks of the participating nations, the D-Mark was effectively the anchor currency, against which other community currencies tried to maintain relatively narrow margins of fluctuation. In effect, this probably increased the international role of the D-Mark already supported by the economic success of West-Germany and the stability of the monetary conditions in Germany.

It needs to be restated that the international role of the D-Mark was never a policy target for Germany and even the D-Mark's anchor role in the European currency model was taken with hesitation particularly by the German Bundesbank. Particularly, in the late 1970s, the Bundesbank was forced to take a larger international role, also in the form of a parallel statement to the US authorities, to stabilize the international foreign exchange markets.⁷ The difficulty of balancing this broader international role and the domestic price stability target in times of uncertainty was clearly stated by the Bundesbank.⁸ Nevertheless, the D-Mark gained an important position in international financial markets and it became the second most important currency with 10-15% of the international reserves and bonds in D-Mark.

The difficulties involved with the international role of a currency and in particular within the EMS were also discussed on the way to Maastricht. Arguably the most pressing issue was the fact that the anchor of the EMS, the D-Mark, was managed by the German Bundesbank that was constitutionally obligated to conduct its policy from the perspective of the German economy, although its policy had effects across the community. Compared to this problem, other issues related to the international role of the D-Mark or the future common currency gained less prominence in the discussions.

⁶ Report to the Council and the Commission on the realization by stages of economic and monetary union in the Community, Luxembourg, 8 October 1970 (Werner Report)

⁷ Joseph Gold (1979). *Legal and Institutional Aspects of the International Monetary System: Selected Essays*. International Monetary Fund. p 290.

⁸ See, for example, Bundesbank Annual Report 1978, Part II International monetary developments and external monetary policy.

Exchange rates in the Maastricht Treaty

In the final form of the Maastricht Treaty, the international monetary and currency system did not receive a prominent role. At the time, the main assumption most likely was that the new common currency would fluctuate freely vis-à-vis other major currencies and their respective roles in the international monetary system would be defined by the large variety of economic actors, public and private, through the international financial markets. However, the Treaty did take into account the possibility that the international monetary system would be changed to something resembling the Bretton Woods system with more formally defined exchange rates.

The Treaty assigned the Ecofin council the power to “conclude formal agreements on an exchange-rate system for the euro in relation to the currencies of third States” (currently Article 219(1) TFEU). In such an arrangement, the central rate of the euro would also be adjusted by the Ecofin. Similarly, Article 219(2) states that in case no formal arrangements are established, the Ecofin “may formulate general orientations for exchange-rate policy“ in relation to other currencies. Unsurprisingly, Article 139(2) (g) excludes non-euro Member States from the decision-making on the exchange rates.

The assignment of the main responsibility for the exchange rate to the Ecofin Council follows the earlier practice in most Member States. Formal exchange rate arrangements have been considered political decisions. Even in the case of the independent Bundesbank, the exchange rate arrangements were decided by the German government, as was also demonstrated by some disagreements, for example, concerning the EMS. The central bank is involved and needs to provide its expertise on the matter, but the ultimate decision is a political one.⁹

Against this background, the ultimate responsibility for the exchange rate-related issues lies with the Council, but the content of this “ownership” is unclear. It is constrained by the need to operationalize it “in an endeavour to reach a consensus consistent with the objective of price stability.” In effect, the Ecofin Council should not use formal or informal exchange arrangements to undermine the price stability objective directly or by putting pressure on the ECB. Furthermore, the ways in which the Ecofin can take charge of the exchange rates are quite formal, as explicated in Article 219 TFEU.

Apart from the Ecofin, also the ECB is directly linked to the international role of the currency. As the issuer of the currency it needs to be involved in all exchange rate frameworks, formal or informal. Article 127 TFEU enumerates the basic task of the ESCB that include “to conduct foreign-exchange operations consistent with the provisions of Article 219”, which makes it the responsibility of the ECB to conduct operations needed to fulfil the arrangements agreed by the Ecofin.

⁹ In the case of the EMS, the disagreement between the Bundesbank and the Chancellor Helmut Schmidt was such that it was only solved by Chancellor Schmidt’s threat to change the Bundesbank act.

In more practical term, the exchange rate issues have been important for the ECB during its first two decades, mostly as a policy indicator or even as a source of shocks rather than as a tool or an intermediate target. The ECB (Eurosystem) has not tried to influence the exchange rate explicitly except for rare occasions and for very short periods of time. This took place, when the euro was at its infancy and faced pressures for a decline in value.

The ECB, particularly in its monetary policy role, is affected by the exchange rate, currency arrangements and also by the broader international role of the euro. For monetary policy, the pass-through of import prices to the consumer prices more generally can be a major policy question. With freely fluctuating exchange rates, the pass-through is both more frequent but also probably not as ‘structural’, i.e. it can be assumed to level out over time if it does not affect the inflation dynamics. Fixed exchange rate arrangements are probably more difficult to assess and contain a more profound risk of imported inflation.

More recently, it could be assumed that developments in international financial flows affect the common monetary policy and its assessments. As the financial flows, including also shorter-term interbank flows, can be very large compared to real economy flows, they can complicate the use of money demand equations and information from the credit markets. The ECB thus needs to be aware of the broader international role of the euro and potential changes therein. The annual report on the international role of the euro is clear evidence of this need.¹⁰

The promotion of the international role of the euro

The Ecofin council does not appear to have taken an active role in promoting the international role of the euro. Particularly the last decade has kept the Ecofin Council quite busy in maintaining any role for the euro, as the crisis has severely threatened the very existence and functioning of the common currency.

Also, the ECB has stated that it does not promote the international role of euro as such, and only follows the development closely with an annual report and other means. It could even be argued that the international role of the euro is not only an important information for the ECB but also to some extent an indicator of the success of the euro area economic policy. Indeed, the decline in the international use of the euro since the eruption of the crisis could have been seen as an indicator of mistrust for the currency. However, it is perhaps more likely that the mistrust does not stem from the ECB’s monetary policy as such but rather from the fiscal policy problems and poor economic growth.

¹⁰ <https://www.ecb.europa.eu/pub/ire/html/ecb.ire201906~f0da2b823e.en.html#toc2>

The hesitation towards active promotion of the international use of the euro could also stem from the risk that it is perceived as competition against the US Dollar and the US Federal Reserve. The central banking community is perhaps slightly more cooperative or even collegial than other parts of economic policy, where the domestic audiences might be lured to focus on “winner and losers” on various economic policy topics. Central banks tend to have long-term relationships with frequent contacts, whereby the approach of winning at the expense of the other is at least carefully disguised.

4. Economic perspective on the international role of the euro

The international role of a currency is not a well-defined topic in economics, making its economic assessment complicated. In the following, I will mention a few perspectives on the issue that could even be defined as different storylines or stylized facts. Their relevance for the contemporary case with the euro can be assessed on a case by case basis.

The economic history is probably the most broadly utilized perspective on the international role of currencies, whereby various stages in the international monetary system have been documented and analyzed. The early monetary models consisted of various metallic-standards and had limited guidance for the present-day discussion. The spreading of the gold standard during the 19th century was linked to the dominant role of the Pound Sterling that provided some stability and safety valves for the international monetary system. The case of the Latin Monetary Union during the latter half of the 19th century sought to facilitate trade between its participating nations and through the same standardizations even wider, but it could be labelled as international currency proper only in a very limited sense.

The most widely discussed and analyzed epoch in the international currency sphere is the shift in leadership from the Pound Sterling to the US Dollar. The actual change in leadership was neither instant or aspired. In a way, the role of the City (of London) never fully recovered from the WWI and the temporary abandonment of the gold standard. The US economy had bypassed the UK economy already earlier, and with WWI also the military hegemony was shifted to the hardly enthusiastic US. Simply in currency terms, both the Pound Sterling and the US Dollar were first linked to gold. The Pound Sterling was backed up by the banking machinery of the City and the might of the Bank of England, while the US Dollar was supported by the thriving economy, vast resources and by fewer worriers about its convertibility to gold. Indeed, the Pound Sterling was among the early currencies to abandon the gold standard during the Great Depression in 1931, which was the final (but probably very necessary) blow to its status.

The position of the US dollar was cemented in the Bretton Woods system after WWII. This led to a different perspective that focused on the functioning of the international monetary system during the Bretton Woods era, formally 1945-1971(3). It was a period of dominance of the US dollar, which arguably and particularly towards the end sowed the seeds for the common currency in Europe. The

instability exported by the US and its controversial geopolitical role were perceived as a source of irritation among the major European states, although perhaps for different reasons. This questioned the arrangement that stressed the bilateral exchange-rates between the USD and the various European currencies instead of a European currency model. This economic-historical perspective to the common currency was also mentioned by the Commission Communication, but it did not provide any economic rationale as such that could be applicable to the present situation.

Turning to more theoretical approaches: various branches of both international economics and monetary economics have some connection to elements that constitute the international role of the currency. In international trade, exchange rates and their fluctuation can have a major explanatory power. Exchange rates can be both sources of stability but also of instability. In monetary theory international pass-through of shocks and impulses can be highly relevant. Exchange rates can also be part of the monetary conditions index that measures the accommodative or restrictive stance of the monetary policy as a function of interest rates and real exchange rate.¹¹ For most central banks this means that they take the exchange rate level as a factor, when they decide about the official interest rates. For large and relatively closed economies such as the euro area or the US, this is a somewhat smaller factor, but still an important one.

The international role of the euro as an indicator of success

From the economic perspective, the international role of a currency could perhaps best be understood as an indicator of success. For example, some even small currencies have gained a substantial role mainly if they have a long history of economic stability and success. The Swiss franc is an example of such type of currencies, and even the German D-Mark had a larger role than could be explained only by its size. This seems to have applied also to the euro. Fairly good economic performance up to 2008 led to a situation where the euro had a role similar to the one the D-Mark had had earlier or even beyond it. It was widely used as a reserve currency, as an issuing currency and as an invoicing currency.

When the crisis questioned the viability of the euro area economic model, and even its existence, the role of the euro declined, and it did so even substantially, in all the aforementioned ways. Arguably, the decline in the position of the euro was the largest in the areas that demand sustainability and credibility. The areas that are more driven by trade were more short-term oriented and hence less affected. In this regard, the view of the longer-term viability and predictability of the euro area were given a major blow.

As the situation of the euro area has calmed down in recent times, also its international role has recovered somewhat. It could also be argued that the massive excess liquidity in the euro area created by the ECB

¹¹ See, for example, N.Ericsson, E. Jansen, N.Kerbeshian and R. Nymoer (1999), Interpreting a Monetary Conditions Index in economic policy. BIS; or Charles Freedman (1996), The use of indicators and of the monetary conditions index in Canada in The Transmission of Monetary Policy in Canada. Bank of Canada.

could and should promote its role as an issuing currency. However, it is perhaps unlikely to counterweigh the full influence of the fact that the euro area remains the worst major economic area from the perspectives of growth, fragmentation and financial stability (loans losses and poor profitability).

5. Conclusions

The EU Commission has raised the issue of promoting the international role of the euro with a Commission Communication proposing further steps towards a larger international role for the euro. The Communication lists several benefits of the international role of the euro but does not provide strong argumentation to back them up. This could partly be explained by the fact that the international role of a currency is not a well-defined area or topic. It has elements of economics, politics, and, particularly in the EU context, also constitutional law.

The constitutional law perspective needs to rely on the Maastricht Treaty. From that basis, the Ecofin Council and the ECB, the most relevant actors in the setting, have chosen to take a passive and informative view on the international role of the euro. One key decision has been to allow a free float of the euro against other major currencies. The ECB has continuously stressed that it neither promotes or hinders the international role of the euro, but it is keen to be aware of the situation. One element is to follow and analyze a set of indicators of the euro's international role. Another element is the knowledge of the use of the euro outside the euro area more broadly, which includes also public and semi-public use of euro as an anchor for the domestic currency or in some cases also as a replacement for it. These uses of euro can be complicated for the ECB, because they involve also political elements.

The Ecofin Council could be considered as the ultimate decision-maker for the international role of the euro, mainly through extending its mandate on the exchange-rate arrangements and also by considering the practices in the Member States before the introduction of the euro. Fundamental currency issues are ultimately political matters that go beyond the more specific mandates of the central banks. Central banks need to be involved in a technical capacity and as the issuers of the currency, and this is also the case with the ECB.

The economic questions involved, and also referred to in the Commission Communication are far from clear or straight-forward. While the international role of the euro could have economic benefits, it could also entail costs and constraints for the euro area. At least the idea of challenging the US Dollar in the international scenery might not bring the stability benefits wished for. However, to the extent that the international role of the euro is an indicator of economic success and prosperity, it clearly is a positive outcome, but not as a target as such but as a proof that the target of prosperity has been better achieved. Following this line of thinking, the proposals of the Commission would perhaps need to be rationalized

for their merits in achieving prosperity not as means of achieving a more pronounced international role for the euro.